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NESS WEEK
July 1

BusinessWeek



JULY 1, 1996

A PUBLICATION OF THE MCGRAW-HILL COMPANIES

\$3.50

THE NEW HUCKSTERISM

Advertising is going
underground as
marketers redefine
what
an ad is
and
where
it runs

PAGE 76



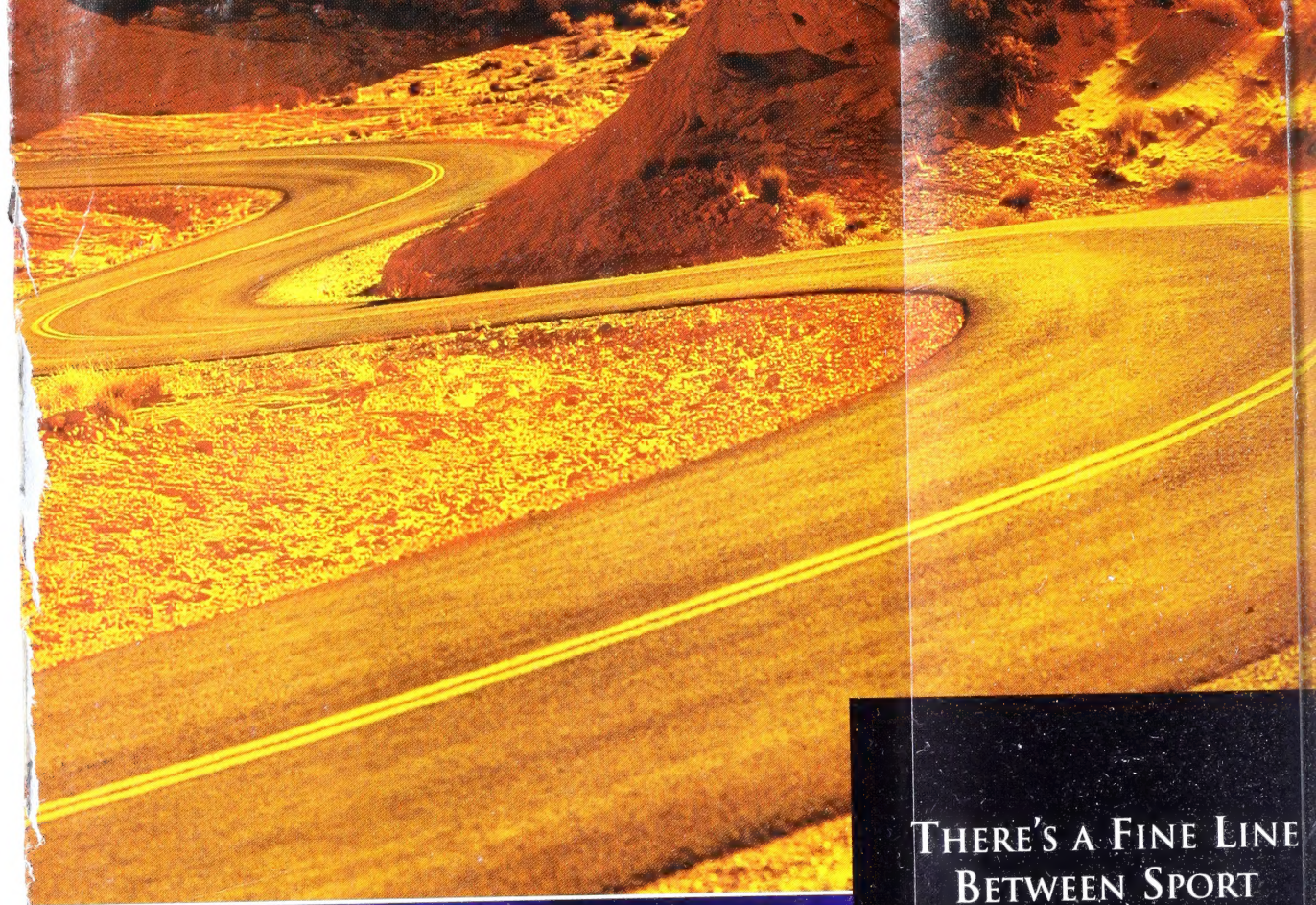
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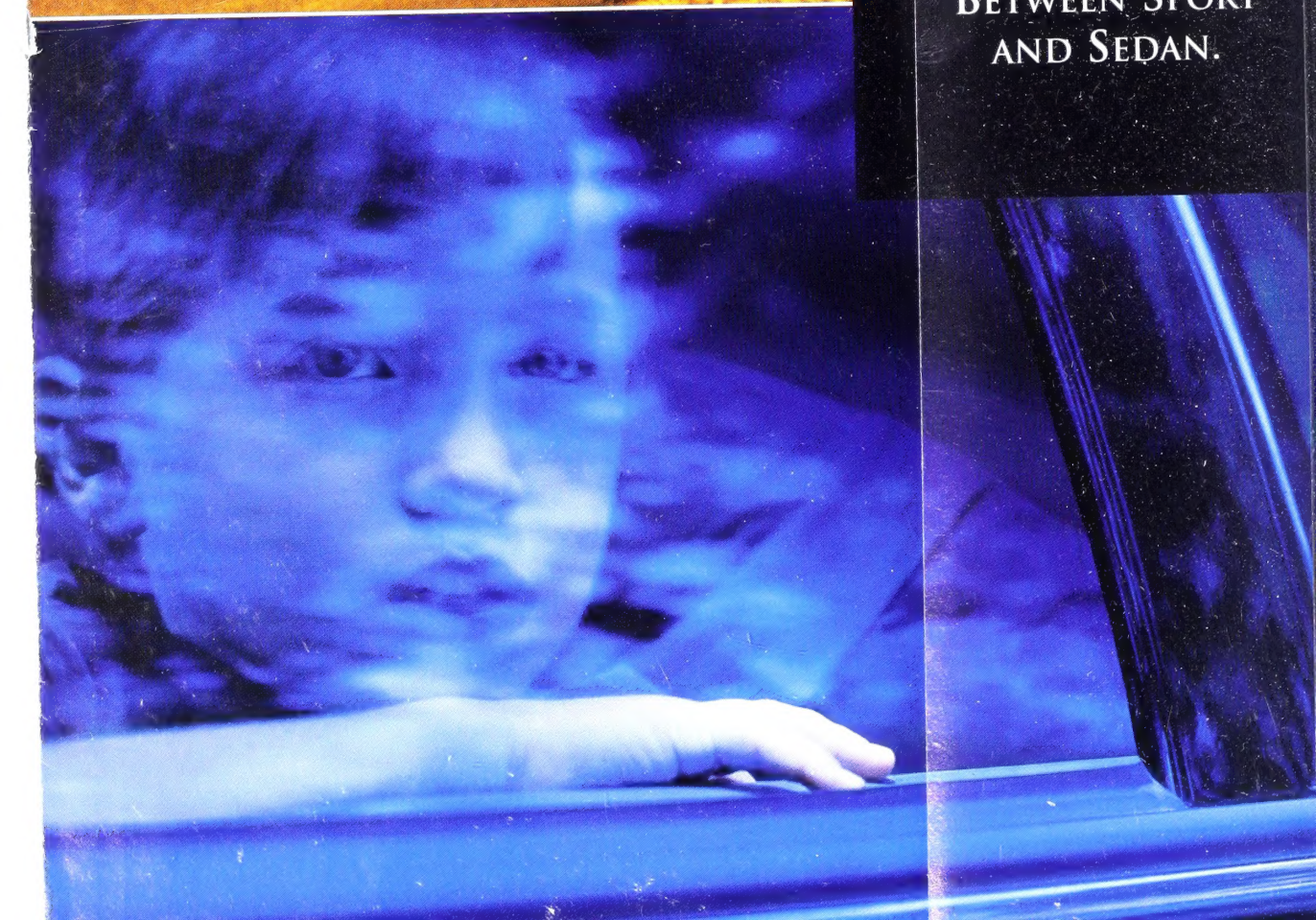
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THERE'S A FINE LINE
BETWEEN SPORT
AND SEDAN.



AS BUSINESS GOES GLOBAL, SO DOES *BUSINESS WEEK*

BUSINESS WEEK has long prided itself on staying close to its readers and leading them into new territory. This is especially true of our international coverage. For major companies, the distinction between national and international business is fast ending. Japan's Toyota, Nissan, and Honda export more cars from plants in America than Detroit's Big Three do. From Seattle, Microsoft Corp. dominates the operating software for personal computers around the world. Germany's Siemens is one of America's largest electronics employers, with 50,000 workers.

Borderless markets and industries defy political boundaries and demand a new sort of journalism. It's no longer useful to talk about how a company is doing in its home country—or even within Europe, Asia, or Latin America—unless you compare it with competition around the world. We call this global benchmarking, and it requires our correspondents to live as specialists in the regions they cover and to use BUSINESS WEEK's worldwide resources to make their evaluations.

It's why we staff 9 overseas bureaus with 18 full-time correspondents and 8 contributing writers, maintain a separate international-finance staff, and have 11 international editors in New York—the biggest commitment of any business magazine.

Each week, we produce three editions. For example, this week's North American cover story is "The New Hucksterism."

The Asian-edition cover is "Acer, Taiwan's Global Powerhouse." And the European-edition cover is "Central Europe." In addition, our writers create an addi-

tional 10 to 12 pages of stories customized for readers in Europe, Asia, and Latin America. They also turn out four pages of international-finance coverage, international editorials and economic analysis, and a regional feature column called Spotlight.

That's now. In August, we'll deepen our coverage when we begin printing the Asian edition in Singapore, which will let us bring more timely Asian stories to Asian readers. Meanwhile, the European edition, printed in the Netherlands, will expand reporting on Central and Western Europe, Scandinavia, and Russia.

Our readers in the U.S. also benefit from our increased international focus. First of all, we are devoting 50% more

space to global coverage. And many of our European and Asian covers are re-edited for U.S. readers. In this issue, the Acer story runs in the Information Processing section, and the Central European story leads the International Business section.

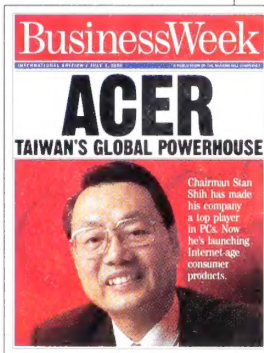
Our goal is to bring you the world's best global and regional business journalism. Says Senior Editor Frank J. Comes, who directs much of this coverage: "BUSINESS WEEK is a much different magazine from what it was three years ago. And it'll be that again in another three years." We hope you approve of the results.

Stephen B. Shepard

Editor-in-Chief



**NORTH AMERICAN
EDITION**



**ASIAN
EDITION**



**EUROPEAN
EDITION**



BusinessWeek

JULY 1, 1996

COVER STORY

NEW HUCKSTERS

They're redefining notion of what an and where it runs
page 76

Cover Story

76 THE NEW HUCKSTERS

Stealth advertising is creeping into a culture saturated with logos and pitches. Shows are starting to look more like commercials, and vice versa. Big companies are trying to look like little ones or become totally invisible. Meanwhile, Liz Taylor appears on four CBS sitcoms plugging her new perfume. Every venue from Broadway to your neighborhood bar has been infiltrated—though you may not have noticed

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Healthy readings on jobs, output, and shopping have economists scrambling to revise their forecasts

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The aftershocks from the company's copper-trading scandal are likely to be long and painful

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It's launching a strong new assault on U.S. markets, targeting autos and personal computers

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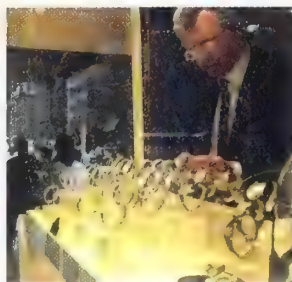
With the market and the economy intertwined than ever, the Fed's gets tougher

PAST PCs
moves to take
ad in a
of

acts



PIT BULL
Ameritech's Dick
Notebaert is
going toe to
toe with
AT&T
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NBC PULLS AHEAD
Its bet on the NBA,
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Investors
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'BUY 'N' BUILD'
It's an LBO
strategy that
works for Hicks
Muse page 86



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anted: A new flight plan for the FAA—
t it won't come easy

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SHOTS, CAMERA, LESS ACTION

agued with lax cost controls,
ollywood studios opt for fewer
roductions

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UPHILL HAUL FOR UNION PACIFIC

es say the rail company's proposed
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LECOM'S TOUGH GUY

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Federico Peña should resign
Don't give Russia the cold shoulder

Up Front

EDITED BY LARRY LIGHT

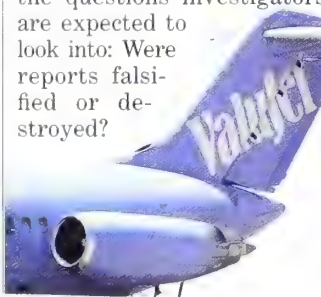
THE FEDS

NOW IT'S A CRIMINAL PROBE AT THE FAA

THE TRANSPORTATION DEPT.'S Inspector General's Office is investigating possible criminal violations at the Federal Aviation Administration regarding its handling of ValuJet. That's according to a government source familiar with the probe who works outside Transportation.

Investigators are looking at whether FAA officials intentionally exercised lax oversight of the low-cost car-

rier before its fatal Everglades crash in May. Among the questions investigators are expected to look into: Were reports falsified or destroyed?



TALK SHOW "The FAA looked at itself in the mirror, and found it needed to make some major changes."

—Transportation Secretary Federico Peña, after the ValuJet crash, on the FAA's plan to focus solely on air safety

Were FAA inspectors or their supervisors threatened? Was mail fraud committed?

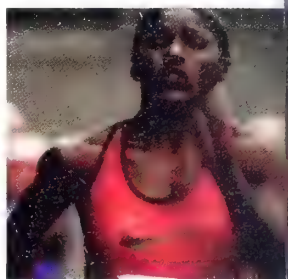
The IG's Office declined comment. The FAA says the IG's Office hasn't notified it about a probe. Certainly, the probe could be downgraded to an administrative inquiry, or axed for lack of evidence. Any criminal case must be brought by the Justice Dept.

Separately, federal prosecutors in Florida are looking at possible criminal activity at ValuJet and at SabreTech, one of its maintenance contractors. *Willy Stern*

SPORTS BIZ

IS NIKE PLAYING OLYMPIC GAMES?

THE TORCH HASN'T REACHED Atlanta, but Olympic "ambush advertising" is a hot issue. This is a recurrent violation for official sponsors who pay up to \$40 million to use the five-ring Olympic logo. Ambushers employ Games imagery in ads without paying the huge freight. *Nonponsor Nike ju*



WARMUP: Torrence's Nike

HONCHOS

NO BOOK YET, BUT LOTS OF SUSPENSE

CEO GIL AMELIO'S MANY problems at Apple Computer don't include writer's block. Less than six months into his new job, he's thinking about penning a book on his efforts to reshape the company.

Shortly before Amelio joined Apple, he published *Profit from Experience* on how he resurrected chip-maker National Semiconductor. Associates

say he's warm to an encore with *Profit* co-author William Simon, a longtime crony. While a deal hasn't been inked yet, Van Nostrand Reinhold, *Profit*'s publisher, says

it's interested. First, Amelio wants more evidence of a turnaround, and he's concerned about the time the book would take. "If we do this, Gil won't be putting any time into it for months," says Simon.

Clearly, Amelio has a way to go before he can crow about anything. Sales remain sickly, losses massive, and the

stock depressed. But he has laid out a strategy, filled key management holes, and propped up the balance sheet.

Nor is it clear that National Semiconductor was a management triumph. In the quarter Amelio left, earnings fell

89% amid a PC slowdown. Worse, 1995 sales grew just 10%—far below industry par. And new Chief Executive Brian Halla has shaken up Amelio's management team.

But author Amelio is in good company. His predecessor at Apple, Michael Spindler, is holed up writing a book, say Silicon Valley insiders. *Peter Burrows*

DEADBEAT NATION

MORTGAGE BANKERS ARE HUMAN, TOO

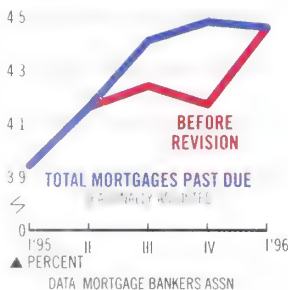
THE ECONOMIC DATA MAY NOT be as bad as you think. The folks who generate one well-watched statistic, mortgage delinquency rates, admit they goofed.

It all started when the Mortgage Bankers Assn. recently issued an unsettling press release about a "dramatic" change in the first quarter's rate, prompting stories that consumers can't handle their debts. The delinquency number measures loans more than 90

days overdue, seasonally adjusted. The MBA's preliminary stats found a huge runup from 4.17% in 1995's fourth quarter to 4.46% in 1996's first period.

Then, the association's chief economist, David Lereah, found that a batch of delinquencies had been omitted from the third and fourth quarters. So the bad surge came last year, and the first period's rate is even down slightly (chart). He canceled a June 13 news conference that was to follow the press release and reran the numbers. "Freak accidents happen," says Lereah. ☐

OOPS, WRONG NUMBERS



AMELIO: No bragging rights

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SLUGFESTS

UNIONS THAT LIVE IN GLASS HOUSES...

WAL-MART STORES, KNOCKED by a union for carrying foreign-made goods, has turned the charge on its accusers. The United Food & Commercial Workers recently went to an East Syracuse (N.Y.) outlet of the nation's largest retailer, which has a Buy American campaign, and found plenty of offending items. But when Wal-Mart visited three supermarkets with UFCW contracts, it also bagged a lot of overseas merchandise.



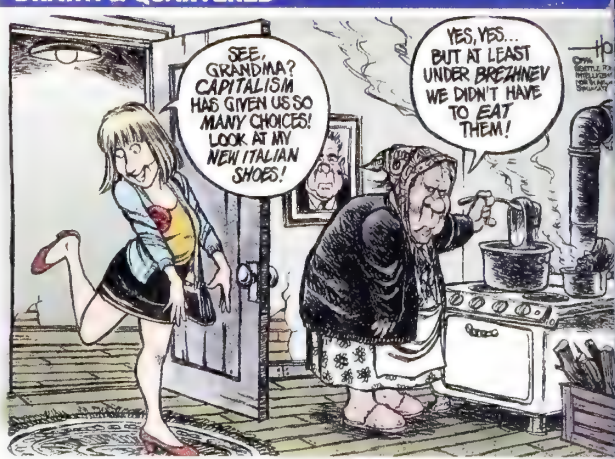
WAL-MART RALLY: Too many foreign goods?

The union brushes aside charges of hypocrisy, saying the countereffort by the usu-

ally mum Wal-Mart shows the UFCW has hit a nerve. Greg Denier, assistant to the UFCW's president, says the union targeted Wal-Mart because "its low standards set the tone for the rest of the retail industry." The UFCW is also concerned about nonunion Wal-Mart's rapid push into groceries.

One UFCW local offered \$500 to whoever found the most foreign labels at the East Syracuse store. The winner gathered 38 different items. At a union rally outside a Las Vegas Wal-Mart, Chinese human-rights

DRAWN & QUARTERED



activist Harry Wu and union leaders denounced the merchandise from China because of human-rights abuses there.

Then, Wal-Mart struck back. It says it found items from at least 30 countries, including China, at a St. Louis UFCW supermarket just two miles from a union local, and at Syracuse and Las Vegas stores. The take ranged from toys to appliances to kitchen utensils. *Wendy Zellner*

CAR TALK

CONSUMERS UNITE.COM

THE INTERNET MAY BE valuable consumer weapon battling Big Business. Look at Charlene Blake's grassroots campaign, launched April, 1995, against Chrysler via a Usenet newsgro-



RECALL: Brake breakdown

(rec.autos.makers.chrysler)

Blake, owner of a Dodge Caravan minivan balked at a dealer's \$2,100 brake-repair estimate and e-listed others with complaints about brake failures. Helped by Blake-generated ammo on the Net, a lawyer filed a class action. Today, most of Blake's cyber-kvetchers are claiming victory after Chrysler's April 16 recall of 350,000 vehicles with the Bendix four-wheel antilock brake system. (Sore skeptics say they won't be happy until they get a check.)

Chrysler won't comment publicly except to downplay Blake's role. Execs say the more important factor was brake-problems probe by the National Highway Traffic Safety Administration, which has no comment on Blake's effort. *Lisa Sande*

AFTERLIVES

'PIONEERS GET AN ARROW IN THE BACKSIDE'

RICHARD FERRIS' DREAM—a one-stop travel supermarket called Allegis—is coming to life again, long after it failed him. He's cheering because



FERRIS IN '88: Allegis died, his idea didn't

another company, HFS, is assembling a '90s version of the concept.

A decade ago, Ferris created Allegis by joining United Airlines, Hertz, and Westin and Hilton International hotels.

But airline workers' ire, Wall Street skepticism, and a takeover attempt squelched the idea. In 1987, Ferris' board ousted him and went on to dismantle Allegis.

HFS is looking for synergies in lodging, real estate, and lately, auto rentals—and getting a more hospitable response. With an empire that includes Ramada and Century 21, HFS is eyeing Avis.

The stock is soaring. Says its chief, Henry Silverman, of Ferris: "Pioneers get an arrow in the backside."

Ferris thinks HFS's concept is "outstanding," with one caveat. HFS franchises the businesses, aiming to be better insulated from downturns. Yet Ferris insists that

owning the units, as Allegis did, makes for better synergy and would have worked with time. Ferris, 59, is still in aviation and hotels, but now he keeps them separate. Based in Chicago, he is co-chairman of Doubletree, which manages 174 hotels. A globe-trotting tourist, Ferris also owns Priestar, an outfit that repairs and maintains private planes. *Randi Feigenbaum*

THE JOB'S IN THE BAG

A rebounding economy is one cause for the optimism of out-of-work executives. Another: a more proactive workforce. Despite growing job creation, downsizing threats remain. So more people prepare for potential layoffs by networking while still employed.



HOW DO YOU FEEL ABOUT YOUR JOB PROSPECTS IN THE NEXT TWO MONTHS?



▲ PERCENT DATA LEE HECHT HARRISON



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a good bottom line
and a better bottom line.

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To say it's got

nice

color

is kinda like saying

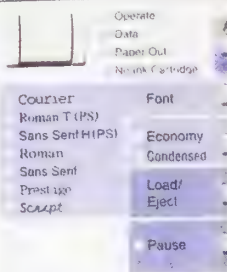
Van Gogh

was pretty good

with a can of paint

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Readers Report

pany goes to extraordinary lengths to inspect each part for condition and proper documentation before it enters our inventory and again before we ship it to the customer.

You seem to think that the FAA should impose more regulations on the airlines. This will do nothing to protect the flying public from bad parts with legitimate-appearing documentation. On the contrary, the need is for regulation of the currently unregulated aftermarket parts suppliers. Airlines need a safe and reliable source of spare parts, not more onerous regulations.

Frederick W. Sine
Executive Vice-President
Avatar Alliance
Stratford, Conn.

After over 50 years in aerospace industry management, I find your lead article to be directly on target. During my years with my father, Donald W. Douglas Sr., we were always very deeply concerned with the issue of counterfeit parts finding their way into use in the world's airlines.

My current organization has developed a system to completely eliminate the counterfeit-parts problem and at the same time reduce airline expense, rather than generate increased costs. However, we have been unable for three years to obtain the very modest funding required from either public or private sources to bring our solution to the traveling public. Unfortunately, it will probably take a Lockerbie-type counterfeit-parts crash to get the action that is required.

Donald W. Douglas Jr.
Chairman
Douglas International Group
Temecula, Calif.

Great story. Thanks for peeling back the curtain that aviation leaders have, with a few exceptions, virtually ignored. The FAA has not created a "uniform, routine, and effective" system for protecting the spare parts inventories used on private and commercial craft. I doubt the system can be flushed clean as long as the Old Guard rules the FAA. This is the gang that promised three Presidents a modern air traffic control system and failed.

In 1989, my daughter, along with 111 others, perished in the crash of United Airlines Flight 232 in Sioux City, Iowa. A defective engine part, a faulty design, and a faulty inspection contributed to her death.

Inventory control remains, as far as I can tell, as sloppy today as it was then.

CORRECTIONS & CLARIFICATIONS

A review of *False Impressions* (Books, June 3) incorrectly stated that the author, Thomas Hoving, suspected that paintings owned by singer Joan Sutherland were fakes. In fact, the paintings belonged to an unidentified collector.

"Caught in the glare of the ValuJet crash" (News: Analysis & Commentary, June 10) misrepresented the name of the company recently acquired by Sabreliner Corp. The correct name is SabreTech Inc.

Let's hope your story stirs some positive changes in the spare-parts warehouses of the world's aviation industry.

Tom O'Mara
Chairman
Aviation Consumer Action Project
Reno, Nev.

VIEWS FROM ALL OVER CREATION

"Monkey business in the classroom" (News: Analysis & Commentary, June 10) tells of how the Cobb County (Ga.) school system requires that creation theory be taught in the classroom. It was my understanding that some years ago the U.S. separated church and state. How can our government, be it state, county, or federal, claim to be separate if they continue to teach religion in schools? Let Cobb County worship in their churches and teach creationism at home. But don't allow them to force their religion into schools.

Tara McDaniel
New York

There are many intelligent, well-educated people in this country who sincerely believe in creation, and they have at least as much scientific evidence to back their beliefs as those who believe in evolution as the origin of life on earth.

To dismiss those of us who believe in creation as scientifically naive or strong in faith but weak on facts is absurd.

Marc E. Rold
Business Consultant
Torgerson Associates
Kalispell, Mont.

Your story exposes the gutlessness of publishers, school administrators, and teachers to stand up for what is right. Thinking parents need to unite with teachers and school administrators to fight the efforts of the Religious Right

to return American education to Dark Ages.

James Wi
Pittsbu

I was quoted out of context in your story. Our organization, Reasons to Believe, is not a creationism advocacy group as most people understand creationism. In fact, we are strongly opposed and are attacked by most creationist organizations. Also, I am not advocating that creationism and evolutionism should both be taught in public education.

Hugh R
Preside
Reasons to Believe
Pasadena, Cal

ACTIONS SPEAK LOUDER THAN WORDS, SENATOR

Contrary to your recent article "Abortion showdown" (Washington Outlook, June 3), which described Sen. Kay Bailey Hutchison (R-Tex.) as pro-choice, she has consistently voted against choice. It is disingenuous for her to portray herself as pro-choice and inaccurate for anyone to describe her as such.

For example, Senator Hutchison voted against providing abortion coverage in federal employees' health insurance and she also voted against Dr. Henry Foster's nomination to serve as Surgeon General.

Kate Michelm
Preside
National Abortion & Reproductive Rights Action League
Washington

HOW TO REACH BUSINESS WEEK

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Chicago Tribune, 6/11/95 "Strategic Vision's"™ 1995 Vehicle Experience Study is based on a total of 31,440 new vehicle buyer responses indicating owner's positive and negative experiences during the first 90 days of ownership. "Strategic Vision's 1996 Vehicle Experience Study"™ surveyed 35,652 Oct.-Nov. new vehicle buyers of 200+ models during the first 90 days of ownership. 1995 Lease: \$399 per month for 36 months. **\$2,600 DOWN PAYMENT.** \$3,448.33 due at lease signing (first month's payment of \$398.33, plus \$450 refundable security deposit, plus down payment). Taxes, license, title fees, and insurance extra. GMAC must approve lease. Example based on Aurora model: \$35,500 M.S.R.P., including destination charge. Monthly payments total \$399.88. Payments may be higher in AL, CA, CT, HI, NY, RI, TX and VA. Option to buy at lease end at price determined at lease signing. Mileage charge of 15 cents per mile over 36,000 miles. Lessee pays for excess wear. You must take retail delivery out of retailer stock by 10/2/96. This is a special GMAC program. See your participating retailer for qualification details.

HIT & RUN

How Jon Peters and Peter Guber Took Sony for a Ride in Hollywood

By Nancy Griffin and Kim Masters

Simon & Schuster • 479pp • \$25

A REAL-LIFE HOLLYWOOD HORROR STORY

It was 1989, and Fred Price had just finished a job interview he would not soon forget. Price, a Hollywood insider who had run the studio operations of both Columbia Pictures Entertainment Inc. and Universal Studios, had been job hunting in New York. Sony Corp. was about to plunk down \$3.4 billion to buy Columbia from Coca-Cola Co. and was looking for someone to head it. But to get the post, Price needed the approval of Walter Yetnikoff, the volatile head of Sony's CBS Records unit. At a lunch at Yetnikoff's New York office, the mood was hostile and dismissive. The meeting—and Price's bid for the job—ended abruptly when a barber arrived and Yetnikoff donned a kimono to have his hair cut.

Why Sony deferred to Yetnikoff, an executive whose Hollywood track record consisted of a few movie soundtracks and who had just returned from treatment for substance abuse at the Hazelden clinic, is still unclear. What is known is that Yetnikoff immediately called a candidate he preferred, Peter Guber, producer of such hits as *Rain Man*—and of \$100 million in losses at a film company he had run for PolyGram.

The story of how Sony blundered into Hollywood reads like a train wreck ready to happen. With Yetnikoff's blessing, Sony hired the ponytailed Guber and his partner Jon Peters, a seventh-grade dropout and onetime hairdresser to the stars. As co-chairmen, they proceeded to take Sony for the ride of its life, wildly bidding up the cost of movies and building the most lavish studio in a town that thrives on lavishness. In addition to annual salaries of \$2.7 million, each man got his own corporate jet. Peters sometimes used his to fly flowers to an actress working in London. Inevitably, they ran up losses the likes of which Hollywood may never see again.

In *Hit & Run*, Nancy Griffin and

Kim Masters skillfully chronicle the lunacy of the deals, personalities, and excesses that made up Sony's Hollywood nightmare. Both are accomplished Hollywood reporters—Griffin formerly at *Premiere* and Masters for *Time*. As they tell the story, Sony's misadventures serve as a cautionary tale for any investor seeking Tinseltown riches. And despite the notorious history of Sony and archrival Matsushita Electric Industrial Co., overseas investors can't seem to resist this glamorous but treacherous business. The current buzz: Korean executives may be behind bids for MGM, now being peddled by banker Crédit Lyonnais. If so, they had better put on their reading glasses.

Lesson No. 1: Find someone who knows the business. To negotiate the deal with Coke, Sony relied on Mickey Schulhof, a PhD in physics who had risen to head the consumer-electronics company's U.S. operations. But Schulhof was hardly a dealmaker, and pitting him against veteran entertainment investment banker Herbert Allen Jr.—representing Coke—was “like putting my Labrador retriever Thunder against a Chihuahua,” Yetnikoff said later. And the \$5 billion in cash and debt assumption that Sony paid for Columbia showed the mismatch. Only five years later, Sony would take a \$2.7 billion write-down to erase the overpayment.

Still, Sony might have weathered the purchase by putting the studio in better hands. Superagent Michael Ovitz, who had brokered the deal by putting Coke and Schulhof together, wanted the job. But Sony resisted his demands: total control, a chunk of stock, and freedom to buy more companies. Ovitz then took

himself out of the running—and walked away with an \$11 million fee.

That left Guber and Peters. Guber, dressed in flannel shirt and jeans, flew to New York and seduced Schulhof with his trademark charisma and a hyperkinetic flow of ideas. In the end, Sony agreed not only to hire the two men but also to pay an astounding \$200 million for their film-production company. Only later did Sony find that it would also have to pay an estimated \$500 million worth of concessions to free the duo from an existing contract with Warner Brothers.

By then, money was no object. Guber and Peters were left alone to spend whatever they wanted to restore Columbia's shopworn Culver City studio and to revive a near-moribund company. Costs spiraled out of control for Steven Spielberg's *Hook*, for the Michael Douglas-produced *Radio Flyer*, and for *Hudson Hawk*, produced by and starring Bruce Willis. None made money.

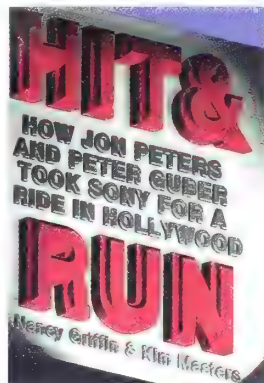
Hudson Hawk alone lost \$42 million for Sony. Emblematic of the prevailing mood was Willis' response to the soaring costs—as reported in *Hit & Run*: “I don't give a s---.”

In the end, it seems, one did. Not Yetnikoff, who was forced out by Sony when his sway evaporated with such key talent as Bruce Springsteen and Michael Jackson. Not Peters, who was shoved out by Guber. And certainly not Guber, who even as he was being forced to resign from the studio he had mismanaged, snagged a package valued at \$200 million to make films for the company. Schulhof was ousted from his Sony post a few months later.

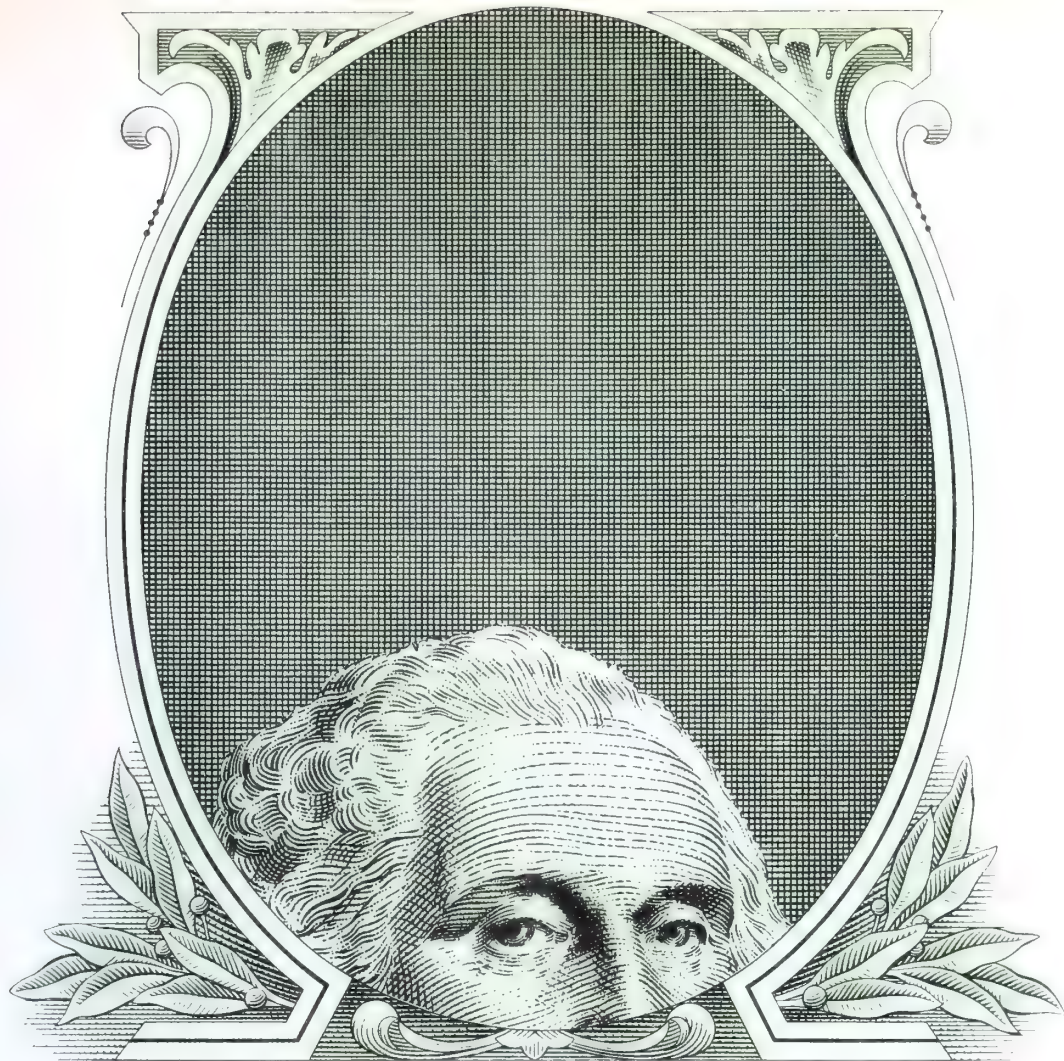
The writing in *Hit & Run* isn't flashy but Griffin and Masters have produced a readable if slightly dated account of one of Hollywood's real-life horror stories. This is no *Indecent Exposure*, David McClintick's brilliant account of the David Begelman check-kiting scandal at Columbia in the '70s. But that was crime, greed, and venality. The Sony story is primarily one of stupidity.

BY RONALD GROVE

Grove is *BUSINESS WEEK*'s Los Angeles bureau chief.



SONY'S MOVIE MISADVENTURES SHOULD GIVE PAUSE TO INVESTORS WITH TINSEL TOWN DREAMS



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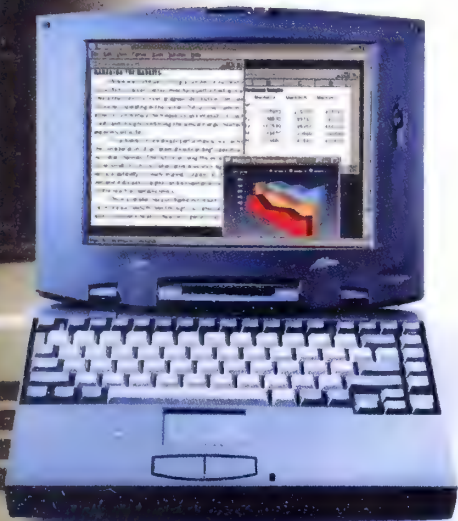
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BY STEPHEN H. WILDSTROM

BROWSERS: THE RACE HEATS UP

Microsoft's new Internet Explorer will give Netscape a run for its money

Not too long ago, a browser was just someone who hung around a bookstore without buying anything. Now, thanks to the World Wide Web and the explosion of Web technology on corporate networks, the browser has turned into a pretty indispensable piece of software.

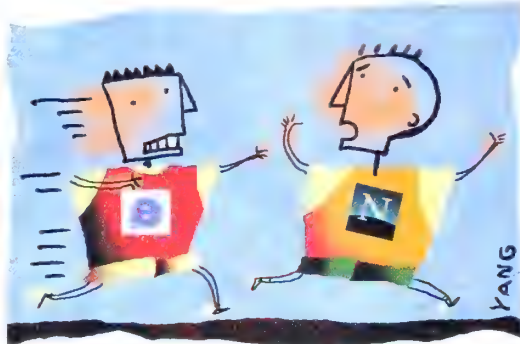
Both Netscape Communications and Microsoft are finishing up work on their latest browsers to navigate the Web. And both have made these once humble programs into versatile tools. (Test versions of the browsers are available for downloading from home.netscape.com and www.microsoft.com/ie/.)

Netscape Navigator 3.0, with commercial release scheduled for July, is an incremental improvement on the already very good 2.0 version. Internet Explorer 3.0, which should be released in late summer, is a huge leap from Microsoft's mediocre current model. This is the first browser that gives Netscape real competition.

GROUP EFFORT. The most notable new feature in Navigator is CoolTalk, which allows voice conversations, typed chat, and the sharing of "white-board" screens. These screens let people take turns making changes in a drawing or in text while others watch.

Netscape has also added a security feature called digital signatures that automatically identifies you to servers, a crucial step for business transactions on the Net. The new browser runs faster, has improved multimedia abilities, and is much more efficient at running network applications written in Sun Microsystems' Java language.

Microsoft's current Internet Explorer 2.0 lacks many of the features of even Netscape's Navigator 2.0,



such as the ability to split a screen into multiple, independent "frames." The new version, however, matches Netscape 3.0 feature for feature—then adds a few of its own. Its basic screen setup, which will instantly feel comfortable to Windows 95 users, is very flexible, allowing you to customize, resize, and move tool bars and menus. In addition to voice, chat, and white-board sharing, Microsoft NetMeeting lets two or more people on the Internet work together in a Windows application, such as Microsoft Word or Lotus 1-2-3. And Internet Explorer has a built-in feature that allows parents to cut off kids' access to undesirable sites.

I have to reserve judgment on several Internet Explorer features, including support for Java and the digital-signatures security feature, because they won't work until a second test version is released, perhaps by the end of June. But a new Microsoft technology called ActiveX does work, and it is likely to pose a major challenge to Java, at least in the Windows world.

JAVA BANDWAGON. The stage is now set for a major battle for your desktop between Netscape and Microsoft. Netscape, which sells primarily to companies, thinks that corporate systems departments will favor Navigator because it offers less reliance on Microsoft and because it works more or less identically on a variety of systems, including Windows, Macintosh, and UNIX. Netscape says that it has no intention of supporting ActiveX. "This is not what we see happening," says product manager Eckart Walther. "In reality, the whole market is moving toward Java."

Microsoft, which is giving its browser away, is appealing directly to end users, whether in the home or in Corporate America. It also has struck deals to make its latest Internet Explorer the browser of choice on both America Online and CompuServe. And by the end of the year, Microsoft will release a new version of Win95 and Windows NT, code-named Nashville, that will make Internet Explorer part of the Windows desktop. Of course, Netscape is betting that you'll prefer Navigator anyway. But if Microsoft can deliver on its promises in timely fashion—always a big if—I'm not sure you'll see any need to go beyond Internet Explorer.

BULLETIN BOARD

CAMERAS

SMALL WONDER

Digital photography isn't much of a threat to film yet but it's moving into the mainstream. The pocket-size Kodak DC20 weighs just 4.2 ounces and costs \$350. A fast lens and imaging system permit indoor photography without flash. The DC20 has some



drawbacks: The camera's memory holds just eight top quality shots, and the relatively low-resolution images don't enlarge well beyond snapshot size. But the included PhotoEnhancer software makes it simple to transfer pictures to a PC or Macintosh and Kai's Power Goo from MetaTools is a fun way to turn Mom into the Wicked Witch of the West—or add other distortions or special effects.

CD-ROMS

FOR THE BIRDS

Bird-watching, among the lowest-tech of activities, gets a boost from the CD-ROM version of the *National Audubon Society Field Guide to North American Birds* from Knopf New Media (800 793-2665). The \$57 program, for Windows and the Mac, contains much of the text of the book and lets you search for birds by habitat, color, size, and geography of species, along with recording of its call. You can also maintain life lists of the birds you've seen. But unless you carry a multimedia laptop, you will want the paper version in your field bag.



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BY GARY S. BECKER

YES, PASS A FLAT TAX —BUT CLAMP A LID ON SPENDING



DANGER:
A flat tax
would be so
much more
efficient than
the current
system that
Washington
would be
tempted to
boost outlays

It's no secret that the U.S. tax system is complex and bedeviled by high rates. Current taxes reduce growth and economic efficiency and divert productive resources into tax avoidance and evasion. So a flatter and simpler tax system could make a big difference. However, to be effective, tax reform must be accompanied by measures to discourage expansion of government spending.

When calculating the effects of tax simplification and lower marginal rates on the economy, supply siders and Keynesians alike assume that government spending is determined independently of the tax system. Recently, *The Wall Street Journal* asked a dozen economists for their views on a flat tax. All supported it, but only a few—I among them—mentioned the potential effects on government spending.

The political process in democracies virtually guarantees that government spending very much depends on the tax structure. Most interest groups have an insatiable desire for government favors. Their demands are kept in check only by taxpayer resistance to shelling out more. If their resistance is weakened by tax reforms that lower compliance costs and reduce the harmful effects on savings and work effort, government spending is likely to rise. Greater spending could cause more economic harm than would be gained from the tax reform.

REAL ESTATE REBELS. The argument that resistance to higher taxes is greater when the burden is heavier and more transparent is supported by the fact that property owners led the tax rebellion in many states. Property taxes are onerous because they are both large and visible. Robert E. Hall and Alvin Rabushka at the Hoover Institution have shown that families could do all their tax calculations on a postcard if the present federal tax system were replaced by a broad-based flat income tax with a 20% rate that exempted families with low incomes. But they do not consider whether such a simpler and more efficient tax system would tempt Congress and the President to raise rates over time to finance old programs and initiate new ones.

My colleague Casey Mulligan at the University of Chicago and I are compiling evidence that shows that tax structure and government spending are rather closely linked. Value-added taxes are flat taxes on purchases that were introduced at low rates in the

1960s. Now, VAT rates exceed 20% in Europe. The result? VATs have permitted a rapid expansion of government spending.

Social Security taxes in the U.S. have rates that apply to the first dollar of earnings. They began in the 1930s at very low levels but they grew over time until combined employee and employer Social Security-Medicare taxes are now close to 15% of wages. The taxes exceed 25% in many European countries. Flat Social Security taxes have been a convenient way for governments to raise an enormous amount of tax revenue. In the U.S. they provide almost as much revenue as individual income tax.

GREATER CONTROLS. The links between tax structure and government spending indicate that tax reform in the direction of simplification and flatter tax rates has to be combined with greater control over government spending. A balanced budget can be a step in the right direction as long as budgets are financed by reducing spending rather than raising taxes.

During recent years, government spending in the U.S. has been constrained by revenue. President Clinton and members of Congress in both parties would have proposed sizable expansion of spending on health and other programs had they not been forced by the electorate to worry about the effect on the budget deficit. Government spending by many members of the European Community would also be larger were they not required to have budget deficits below 3% of gross domestic product before they will be admitted to the monetary union planned for the end of this century.

But additional ways are needed to limit overall government spending, especially if flatter taxation is introduced. In the U.S. Congress could establish an upper limit on the ratio of total federal spending to GDP, a limit breachable only during wartime and other emergencies. Or it might cap federal tax at their present ratio to GDP except when a super majority, perhaps 60% or more of congressional members, support a higher ratio.

Unless they are combined with better controls over government spending, the large benefits from a flatter, simpler tax are likely to be squandered in wasteful expansion of spending on industry subsidies, agricultural welfare, and other politically powerful programs.

Gary S. Becker, the 1992 Nobel laureate, teaches at the University of Chicago and is a Fellow of the Hoover Institution

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BY GENE KORETZ

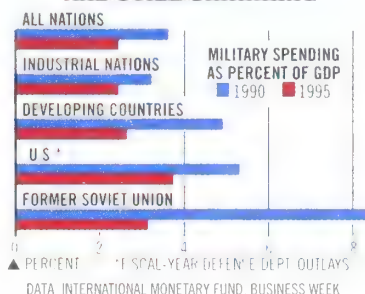
FEWER GUNS, MORE BUTTER

Peace dividends seem to pay off

Global military spending, which turned down in the late 1980s, has continued to decline in the 1990s. According to a new International Monetary Fund report, such expenditures fell from 3.6% of the world's gross domestic product in 1990 to just 2.4% in 1995.

Major catalysts have been the end of the cold war and economic convulsions in the former Soviet bloc. Since 1990, U.S. defense spending—one-third of world outlays—has fallen from 5.3% of GDP to 3.5%. And military spending in

WORLD MILITARY OUTLAYS ARE STILL SHRINKING



the former Soviet Union plummeted from 8.4% of GDP to 3.1% last year.

But the most impressive aspect of the drop is its global nature. Of nations studied by the IMF, only 25 upped their military budgets during the first half of the 1990s (by an average of 0.8% of GDP), vs. 90 countries that cut them (by an average of 1.6%). Of 17 industrial nations, only one—apparently Japan—raised outlays relative to its economy.

A key question is whether the money saved on military budgets has been used wisely. According to the IMF, the annual “peace dividend”—the added amount that would have been spent if military outlays as a share of GDP had stayed at 1990 levels—comes to a hefty \$345 billion. And signs suggest that such savings have often been put to efficient use. “Countries that made sharp cuts in military spending,” the IMF reports, “have also tended to reduce nonmilitary spending and their overall fiscal deficits while boosting social spending.”

By contrast, the few countries that have raised military outlays have also tended to increase nonmilitary spend-

ing and fiscal deficits while reducing capital spending—“suggesting that military spending may be crowding out both private and public investment.”

ARE RATE-HIKE FEARS EXCESSIVE?

Why stock prices may still rise

Concern that the Federal Reserve will soon change course and raise interest rates has begun to spook the stock market. But the belief that such a move would spark a major sell-off are exaggerated, says Leslie Kogod of Capital Investments International Inc.

Kogod's analysis of market moves during the 10 major interest-rate cycles since 1954 shows that in 8 of those cycles stock prices posted above-average gains (up 5.3% on average) in the three months prior to initial Fed tightenings. On the two times the market fell prior to the first Fed funds hike, the declines averaged a modest 1%.

Stock prices did even better in the periods following the Fed's initial rate hikes. In 8 of the 10 cycles referred to above, the Standard & Poor's 500-stock index continued to rise—by an average 5.6% after three months and by an average 8.8% after six months. (On two occasions, the market fell—but by no more than 5% within six months.)

Thus, rather than a response to inflation and overheating, says Kogod, initial rate hikes have usually been an effort to stave off those developments and an acknowledgment that economic growth is good. “Typically, the periods surrounding first tightenings have carried good returns and remarkably low risk.”

BAD TIMES MAY BE GOOD FOR YOU

Death rates drop during recessions

It seems a foregone conclusion that economic contractions are harmful to one's health. Incomes decline, laid-off workers feel anxious and depressed, and many lose their medical insurance.

Yet this thesis—that health suffers when economies slow—is challenged by a new study by economist Christopher J. Ruhm of the University of North Carolina at Greensboro. Ruhm looked at mortality data for all 50 states from 1972 to 1991, comparing changing economic conditions with mortality rates

from 10 causes of death—including car crashes, suicide, homicide, cancer, pneumonia, and heart and liver disease.

The results were surprising. Ruhm found that deaths from 9 of the 10 causes fell when unemployment rose. (Only suicides rose during recessions.) The effects were strongest among 20- to 49-year-olds, the group most affected by changes in economic conditions.

Why would deaths decline in hard times? In the case of car crashes, Ruhm notes that reduced incomes may curb some people's driving and alcohol consumption. And other folk may benefit from a drop in job-related stress. After all, it is a documented fact that heart attacks are particularly common on Monday—the day people return to work.

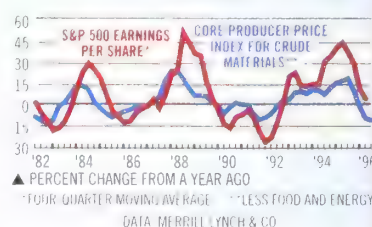
THE MESSAGE IN MATERIALS PRICES

They augur slower earnings growth

After three years of double-digit gains, corporate earnings growth is about to slow sharply, predicts Bruce Steinberg of Merrill Lynch & Co. He sees S&P 500 earnings per share rising just 4% in 1996 and 3% in 1997.

One clue, says Steinberg, is a decline in the producer price index for crude materials less food and energy. The ce-

FALLING COMMODITY PRICES: A BAD OMEN FOR PROFITS?



crude PPI, which reflects industrial materials prices, has fallen 12.5% below its year-earlier level—its steepest drop in 14 years. And the PPI's year-to-year trend has an unusually tight fit with changes in S&P 500 earnings (chart).

Indeed, every time since 1978 the crude-materials prices dropped below their year-earlier level, S&P 500 earnings followed suit. The reason, says Steinberg, is that such prices are a sensitive measure of both corporate pricing power and demand for business output. In short, the core PPI points to a sharp slowdown in economic growth and related earnings momentum that Merrill Lynch sees just around the bend.

BY JAMES C. COOPER & KATHLEEN MADIGAN

A PRICEY STOCK MARKET MAKES THE FED'S JOB TOUGHER

U.S. ECONOMY A soft landing is always a delicate maneuver for the Federal Reserve. But this time, if the economy really is picking off again and raising inflation fears, bringing it back down will be doubly tough. Not only will the Fed have to steer the economy clear of recession; it will also have to avoid wrecking the stock market.

The problem is thorny, because the market and the economy are more intertwined than ever. With a record 40% of adults now owning stock, the raging bull market has pumped up the value of consumer assets, offsetting the negative effects of heavier debts. Since households are wealthier, outlays for housing, cars, and other big-ticket items have benefited. The market's stupor also has financed a capital-spending boom, a key engine of this expansion. If the market tanks, it could take the economy with it.

Sound premature? Maybe. But it's a scenario you should think hard about, because it may be playing out a lot faster than you realize. Based on the data through May for industrial production, retail sales, hours worked, and other measures of activity, economic growth appears to have accelerated to 4% in the second quarter, from 2.3% in the first and 1.3% for

all of 1995. What's more, this new momentum may well spill over into the second half (page 26).

If so, this summer will be decision time for the Fed—to hike or not to hike short-term interest rates. Higher long-term rates, with 30-year Treasury yields at 6.5%, have already caused stocks to lose some of their luster, as bonds offer increasingly attractive yields. The major stock indexes have barely gained ground since interest rates began to rise in February.

LONG RATES CONTINUE to push toward 7.5% or higher—a sure bet if the Fed lifts short rates—the Standard & Poor's 500-stock index would become well overvalued at the current level of 665, according to Morgan Stanley & Co.'s stock market valuation model. That's true even at Wall Street's optimistic expectation that operating earnings for the S&P will come in at \$11 per share, which seems unrealistic given that earnings growth is already slowing from a year ago.

One back-of-the-envelope valuation method, based on the inverse of the 10-year Treasury bond yield,

says that the market is already overvalued. With the 10-year yield at 6.9%, this estimate says that the market's "fair value" at which stocks and bonds are equally attractive is about 14.5 times earnings. Since the S&P currently stands at 16 times expected earnings, the market is 10% overpriced.

Stock market fragility is a big reason the Fed will have to be super careful with interest-rate policy in coming months. The key question—not only for the Fed but also for the financial markets—is: Will the economy slow down enough in the second half to assure that wage and price pressures do not start building?

The Fed's June 19 report from its 12 regional banks on economic conditions, prepared for the July 2-3 policy meeting, noted expanding activity generally, with several regions saying that "the pace of growth accelerated recently." Most districts reported tight labor markets, and many mentioned rising prices for some raw and intermediate materials.

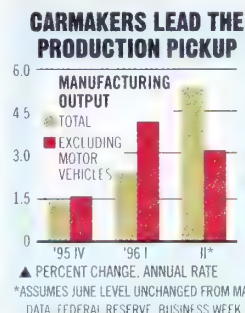
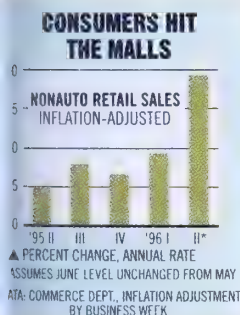
Still, the report said that evidence of faster wages and retail prices was only scattered. But if the economy's growth trend is shifting to more than 3%, idle production capacity will quickly dry up, and the already-low unemployment rate will go even lower.

Fed Governor Lawrence B. Lindsey recently told Reuters news service that, with the unemployment rate in the 5.4%-to-5.6% range for more than a year, the Fed essentially has been "experimenting" with a lower noninflationary jobless rate than anyone thought possible. But if the economy is revving up again, it's hard to believe that the Fed will remain comfortable when joblessness dips further.

BLAME THE RECENT ECONOMIC DATA for the growing speculation about Fed tightening. It all began with the May report of surprisingly brawny labor markets, and the latest numbers on retail sales and industrial production only fuel the discussion even more (charts).

Consumers seem raring to spend. Retailers said that their May receipts rose a sturdy 0.8%. Excluding strong auto sales, the tally was up a smaller 0.3%, but nonauto sales had jumped 1.1% in April. Adjusted for inflation, nonauto sales in the second quarter are on a track to post the best quarterly showing in 3½ years.

Car buying is also brisk. The May annual sales rate



for domestic and imported cars and trucks stood at 15.8 million, matching the year's best showing. Through May, vehicle sales are running about even with their burly first-quarter average. Overall consumer spending, some two-thirds of the economy, could rise 3% or more for the second quarter in a row.

WITH DEMAND HOLDING FIRM, manufacturing output is more likely to accelerate than to fade. In fact, output is already speeding up. Industrial production in manufacturing, mining, and utilities rose a solid 0.7% in May, with manufacturing output alone up 0.5%. For the quarter, factory production so far is rising at an annual rate of greater than 5%, double the first-quarter pace.

The March strike at General Motors Corp. has distorted the pattern of output with first-quarter weakness followed by a second-quarter surge, but durable goods production generally is strengthening. In particular, output of computer equipment continues to rise at 40% per year. Also, recent weakness in nondurable manufacturing appears to be bottoming out.

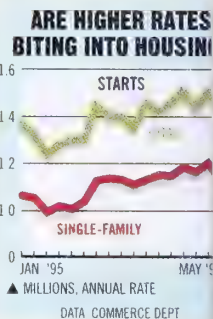
Overall, industry used 83.2% of its output capacity in May, up for the second consecutive month. The level is already higher than the rate that existed in early 1994, when the Fed began its last tightening cycle.

Recent reports on housing are about the only glimmer of hope that higher long-term rates are starting to

cool activity. But even there, the evidence is hardly conclusive. Housing starts fell 4.7% in May, to an annual rate of 1.43 million (chart). Still, starts remain at a high level: So far in the quarter, they continue to be slightly ahead of the first-quarter average.

In June, homebuilders surveyed by the National Association of Home Builders noted that current sales edged lower, but that builders' expectations of future sales rose. As yet, there is no evidence from the weekly reports on mortgage applications that home buying has tapered off. Application volume in early June was even a shade higher than it was in January, when mortgage rates were a full percentage point lower.

The fact is, mortgage rates have been only one of the supports under housing. Solid growth in jobs and income, high consumer confidence, and especially the wealth effect from the stock market gains have played key roles as well. But for the second half, all the money that has been pouring into mutual funds may be at risk. So, if push comes to shove at the Fed this summer, and the policymakers hike rates, make sure you keep your stockbroker's phone number handy.



JAPAN

WEAK LINKS IN A STRONG RECOVERY

The Japanese economy shot up like a rocket in the first quarter. But that only heightens fears that policymakers will start to raise interest rates.

Real gross domestic product

surged at a 12.7% annual rate in the first quarter, the strongest in 23 years (chart).

Special factors inflated the gain. Fiscal stimulus added 13.8 trillion yen (\$130 billion), and an extra day in leap year pushed up growth by one-half percentage point, said the Economic Planning Agency. Still, all sectors except trade grew, verifying that Japan is in a solid recovery.

The consensus forecast expects real GDP of 2.4% in 1996, and the latest Tankan survey shows that

business prospects are creeping up, with improved earnings and inventory levels, and sharply higher investment plans. Better profits reflect the windfall for exporters from the weaker yen. It

dipped below 108 to the dollar after the GDP report.

The second quarter looks positive for Japan's industrial sector. April production was up 0.3% from a year ago, and machine orders jumped 26.7% from March, double expectations. But the

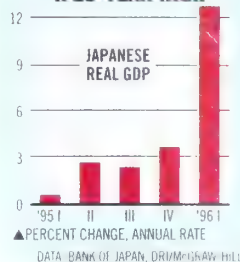
trade surplus, down 60.5% in May, remains a drag on growth.

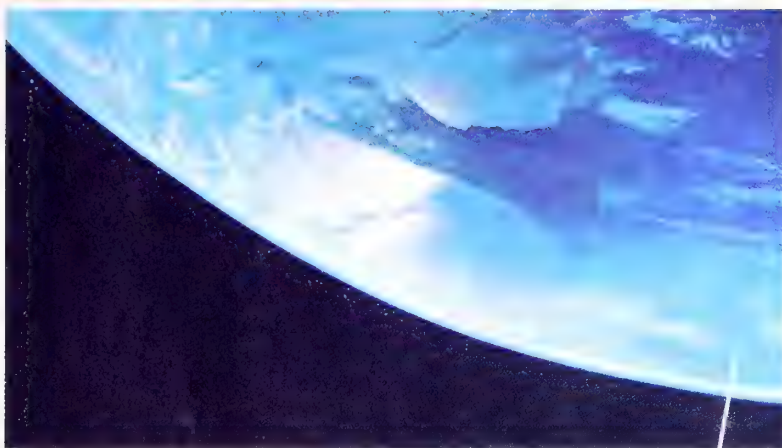
The GDP surprise heightens speculation that the Bank of Japan will lift short-term interest rates. BOJ Governor Yasuo Matsushita

has said that policy "will continue to aim at bolstering the recovery with the goal of a 'self-sustaining' upturn. But press reports on June 19 suggested a hike could come as early as July. Still, domestic demand must continue to grow to keep the recovery going. The Tankan results suggest that business spending will remain on an uptrend this year, and the weaker yen means exports will become more price-competitive later on.

But consumers remain shaky. Their spending rose last quarter, but the gains weakened in each month of the period. And unemployment returned to a record 3.4% in April, from 3.1% in March. Policy must be geared to improving the economic status of consumers. Only then can Japan realize the goal and benefits of a self-sustaining recovery.

GROWTH SURGES TO A 23-YEAR HIGH





JUST ONE OF 78 WORLDWIDE DESTINATIONS WE FLY TO

Quietly, year by year, our list of destinations has steadily grown. This year, we will carry almost 23,000,000 people across five separate continents, to 78 cities. Which, we must immodestly point out, not only makes

us one of the fastest growing airlines, but also one of the world's top carriers. **It's just one more pleasant surprise you'll find with Korean Air, and one more reason you should fly with us.**

KOREAN AIR

BEYOND YOUR IMAGINATION

THE ECONOMY

HAVING A HEAT WAVE

All of a sudden, the tepid economy is really cooking

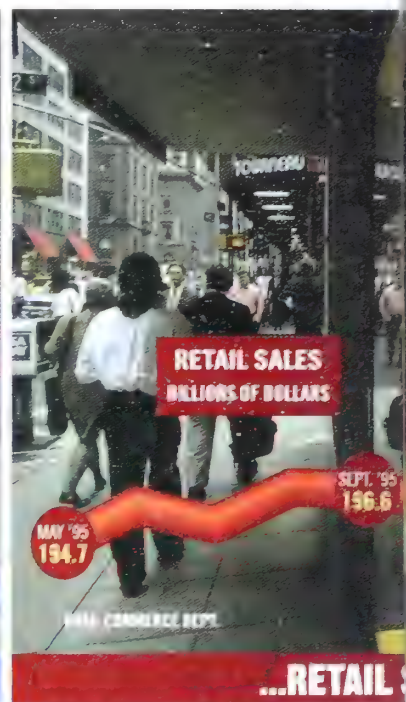


So much for slow and steady. At the end of 1995, forecasters looked into their crystal balls and saw a 1996 economy humming monotonously along at a 1.9% annual rate in each quarter. Then something happened that surprised just about everyone. Economic activity in the first quarter grew at a solid 2.3% clip and threatens to barrel through the second at 4%—with enough momentum from inventory rebuilding to blaze through the autumn.

Such an extended gallop upsets a lot of recent expectations. It raises the prospect of higher wage and price growth, for one thing, which would leave the Federal Reserve little choice but to slam on the brakes harder than anyone expected just a few weeks ago. Odds of a recession next year are still below 50%. But instead of the slogging-

but-consistent expansion many had expected, the emerging economic scenario may mean a cycle of the mini-booms and -busts that can make life miserable for company executives.

"SNEAK ATTACK." The economy's current strength is undeniable (charts). Industrial production increased by 0.7% in both April and May. Payrolls are rising at a monthly average of 220,000 so far this year, up from 185,000 in 1995. And retail sales advanced a healthy 0.8% in May. Little wonder that the *Blue Chip Economic Indicators* survey of economists says that the consensus forecast now expects second-quarter GDP growth of 3.3%, a significant rise from 2.3% projected in April. The most optimistic have penciled in growth of 4% or more—far above the 2.5% rate thought to be the Fed's limit for noninflationary growth.



What happened? Until recently, many signs augured poorly for such a strong expansion. Long-term interest rates have been rising sharply since December, with the yield on 30-year U.S. treasuries up by more than a percentage point, to 7.10%. Mortgage rates are climbing, too, with the 30-year fixed rate on loans up to 8.57% in mid-June. In theory, higher borrowing costs should slow demand, especially for big-ticket items such as cars and housing.

Not this time. "The sneak attack [GDP] forecasts came from the strength in auto sales," says Michael R. Engle, chief economist at MMS International, one of the McGraw-Hill Companies. So far this quarter, sales of domestic-made cars and light trucks are running equal to the sturdy 13.5 million average of the first quarter. Carmakers, thou-

expected a modest sales gain this year, so they spent the winter trying to trim their inventories. The March strike at General Motors Corp. did the job better than Detroit had planned. Now, a game of catch-up, auto production could add two percentage points to growth this quarter.

fleets of sedans and minivans only part of the story. Even with higher interest rates and a record tax bill of \$75 billion in April, consumers are buying. Retail sales excluding cars are growing faster in the second quarter than they were in the first. In May, department stores, building-material suppliers, and furniture merchants rang up big sales increases. Even the struggling apparel

a lot of overtime this summer. "The month of May was a relative boomer and June seems equally strong," says Steven C. Riedel, vice-president for marketing and product management at the division. "We feel pretty positive about the balance of the year."

Demand from the corporate sector is also going gangbusters. Healthy profits and a surging stock market give businesses the cash to spend on more productive equipment. "We continue to see robust growth in electronic capital goods—between 15% and 20%—which, from a historical standpoint, is quite high," says Vladi Catto, chief economist at Texas Instruments Inc. Output of business equipment, from low-tech gas tur-

makers will lift the federal funds rate, now at 5.25%, by a quarter point at the Aug. 20 meeting. And MMS's Englund for one sees another quarter-point lift in September. Fed insiders, however, say it won't worry about growth as long as inflation indicators stay in check.

The growth surge hasn't tripped any inflation circuits yet. Ruthless bargain-hunting by consumers is one reason, as are productivity gains that are keeping labor costs low. Economists expect consumer prices to increase just 3.1% for all of 1996.

Many economists now don't expect a slowdown before the fourth quarter. By then, they assume, inventory rebuilding will be done. Higher mortgage rates



CLIMBING...

er shows signs of a pulse this spring. Americans may kvetch about economic anxiety, but the fact is that jobs and wages are up solidly this year. Confidence is high. And the stock market has given consumers the financial wherewithal to take on \$37 billion in new debt in the first four months of 1996. At a Honda dealership in Shelton, Conn., sales have been "unbelievable" since Honda introduced financing packages in January, says general manager Ed Desjardis: "There are lots of people who have the means and they've just been waiting for a deal."

Increased demand, though, has caught many businesses by surprise. General Electric Co.'s appliance division, for one, expected a flat year industrywide. Instead, demand is up about 4% from a year ago, and GE workers are looking at



...AND EQUIPMENT BUYING IS UP

binaries to high-tech textile looms, is up a sturdy 8% from a year ago.

The demand shock has left inventories low compared to sales. So manufacturers are gearing up production to restock warehouses while also filling new orders. Inventory rebuilding is why some economists expect a robust third quarter, with GDP growth at 3% or more.

HAWK SQUAWK. All this activity, of course, has not gone unnoticed by inflation hawks roosting in the bond market. Keep this frenzied pace up, they warn, and faster inflation will be hot on its heels. Price pressures have to be a concern, what with unemployment already at 5.6% and capacity use on the rise.

For now, though, the Fed is unlikely to raise short-term rates at its upcoming July 2-3 meeting. But expectations on Wall Street are increasing that policy-

will have sufficiently slowed housing starts, and weaker profits will put some capital spending on hold. As for consumers, increased credit problems will curtail borrowing. Delinquency rates for credit cards hit a 15-year high in the first quarter, and households are using a record 11% of their aftertax income to pay off old installment debts.

And next year? The big danger remains that inflation fears will somehow spook the bond market. In that event, bond yields could head above 7.5%, forcing the Fed to hike rates faster than planned. Such concerns make next year's outlook dicey. At the very least, the economy's strong run this year is likely to leave it short of breath in 1997.

By Kathleen Madigan in New York, with Zachary Schiller in Cleveland, and Gary McWilliams in Houston

SCANDALS

DESCENT INTO
THE ABYSS

How the copper-trading affair engulfed Sumitomo



The world has witnessed numerous spectacular financial scandals, from the Ponzi schemes of the 1920s to the rogue futures trades that ate up Barings PLC. But the Sumitomo Corp. copper-trading scandal is likely to go down in the history books as perhaps the most audacious yet.

Hard to believe it all started with an unassuming 48-year-old copper trader in Tokyo. For a decade, Yasuo Hamanaka, an assistant general manager of the nonferrous metals division at Sumitomo, was the puppet master who pulled the strings of traders in the "copper ring" at the London Metal Exchange (LME), which sets copper prices worldwide and bent a \$1.45 trillion market to his will. Market sources and regulators now suspect he was trying to corner the market with the help of a cadre of brokers, traders, and other accomplices, using several offshore bank accounts to bury his losses. Incredible as it seems, his market-rigging schemes existed right under regulators' noses. Sumitomo's losses so far amount to \$1.8 billion, and the figure could go higher.

"ALTERED" REPORTS. Now, the consequences of the scandal are spreading in ever-widening gyres. A company the size of Sumitomo's can absorb the losses, but it has \$34.8 billion in assets and \$133 billion in sales last year. But the fair has led to criminal investigations related to the scandal in London, New York. And the aftershocks may eventually reach into the company's executive ranks. Three LME board members tell BUSINESS WEEK it's inconceivable Sumitomo officials did not know the extent of Hamanaka's trades. "There is nothing Hamanaka was doing that wasn't done with the intimate knowledge of senior people at Sumitomo," says one. Adds another: "They knew what he was doing. They knew what risks he was taking."

Sumitomo President Tomiichi Akai

IRIAN JAYA
MINE

The market-rigging case may reach into the top ranks of Sumitomo, the world's No. 1 copper supplier

ma said at a press conference in Tokyo that Hamanaka showed his superior "partially altered" reports. The company revealed on June 1 that it had fired Hamanaka, and is cooperating with investigators.

Regulators won't come away scathed. The scandal is battering the credibility of the London Metal Exchange

ere 88% of the world's listed copper attracts are traded. A U.S. regulator is the exchange stonewalled the commodity Futures Trading Commission for months. "They didn't want to know about the situation. We have a sense of urgency that's different about regulation in this country," he says. Steve Rhinds, senior editor of *Metals Week*, like *BUSINESS WEEK* a McGraw-Hill Companies publication, blames London's lax system of self-regulation. "All the third members of LME are also members of trading companies," he says.

The upheaval also is likely to spread to Chile, where the state-owned copper company, Codelco, is still trying to figure out how it was decided of \$200 million in 1994, in circumstances allegedly involving some of the same individuals at the heart of the Sumitomo case. Says Codelco Vice-President Juan Eduardo Herrera: "The credibility of the LME is in question, and we will have to see if the market and its authorities are respected after this."

How did things come to such a pass? The tale begins in 1986, when Sumitomo was chosen to lead a team of copper futures traders. Sumitomo eventually was allowed to amass large positions, and he had signing authority over several bank accounts where large sums of credit smoothed the way. Traders speculate that he was given latitude because of his solid reputation after 20 years in the division.

SQUEEZE. The first sign of trouble came in 1991, when copper broker David Threlkeld received a letter—allegedly from Sumitomo—asking if he would fake trade confirmations for a fake deal worth \$425 million. Threlkeld refused and gave the letter to LME Chief Executive David King. While Threlkeld says he was told by King that he was not to get sued for the letter, he insisted in an interview with *BUSINESS WEEK* that the LME investigated

but that the matter was outside its purview. Threlkeld saw other suspicious activities. In 1992, for example, he warned Britain's Securities & Futures Authority (SFA) of a single copper transaction involving 20,000 tons, at the time worth \$80 million, and heavily in favor of one of the four parties in the deal. The LME and the SFA decline comment on whether they took any action.

houses, among them Sumitomo. Market sources now believe Hamanaka created such a squeeze for most of the past year. Philip Adeane, managing director of London-based Antofagasta Holdings, owner of Chile's Los Pelambres copper mine, says that in his personal opinion Hamanaka "kept the price of copper at an unrealistic level for over a year. He basically managed to corner a part of the market."

It wasn't until October, 1995, that Hamanaka's actions drew the ire of U.S. regulators at the CFTC. And this time, the market anomalies also roused R. Patrick Thompson, president of the New York Mercantile Exchange, who wrote to the CFTC expressing concern. The LME's King contends that Thompson's motive for getting involved may be resentment of the trading volume LME has won from Thompson's exchange. Still, CFTC enforcement officials pressed London and Sumitomo to investigate. They did—and in early April, Sumitomo agreed to make Hamanaka available to the CFTC.

At that point, things really came to a head. Hamanaka was deposed at New York's glitzy Waldorf-Astoria Hotel, chosen because the hotel would accommodate the chain-smoking Hamanaka's habit. A second deposition was set for mid-June, but Hamanaka confessed to Sumitomo on June 5.

One lesson to be learned from the Sumitomo affair is that it is clearly impossible for any player to defy market

forces for very long. But it's also a cautionary tale for management and regulators: Whether what's traded is copper, bonds, or Nikkei futures, the markets will only function as well as the people charged with keeping them clean and fair.

By Paula Dwyer, with Heidi Dawley, in London, Greg Burns in Chicago, Brian Bremner in Tokyo, and Dean Foust in Washington

DESPERATION IN THE PITS



METALS TRADE: Fast and furious, but how fair has it been?

NOVEMBER, 1991 U.S. broker David Threlkeld informs the London Metals Exchange that Sumitomo's Yasuo Hamanaka asked him for a backdated confirmation on \$425 million in fake trades. The LME claims it found nothing wrong within its jurisdiction.

SEPTEMBER, 1993 A copper "squeeze" develops: Despite plentiful supplies, spot prices are higher than the three-month futures price. The LME fingers Hamanaka; he denies manipulation.

OCTOBER, 1995 Pricing anomalies again appear and rumors circulate that Hamanaka has locked up a large chunk of the supply. The Commodity Futures Trading Commission begins investigating.

NOVEMBER, 1995 Patrick Thompson, head of the New York Mercantile Exchange, warns that copper in the LME's Long Beach (Calif.) warehouse is piling up "and may be part of a squeeze or other market misconduct." The LME starts investigating Hamanaka.

APRIL, 1996 CFTC authorities inform Sumitomo that they have uncovered irregularities in the company's trading accounts.

MAY 17, 1996 Sumitomo pulls Hamanaka back from his position as top copper trader and confirms the move after traders hear of it.

JUNE 13 Sumitomo announces losses of \$1.8 billion.

DATA: *BUSINESS WEEK*

From 1992 to 1995, LME officials and regulators occasionally asked member firms trading on Hamanaka's behalf to come and discuss his activities in the market. One scheme that repeatedly caused havoc, traders say, involved piling up copper in exchange warehouses, leading to a supply squeeze that drove up futures prices. This would drive up the value of copper stocks, benefiting the owners of the copper in the ware-

TRADE

THOSE FOOTSTEPS YOU HEAR ARE JAPAN INC.

It's about to launch a strong new assault on U.S. markets

Japan's economic slide this decade has given many Americans a sense of quiet delight. Japan in the late '80s was the touchstone of U.S. economic anxiety, but it turned out to be an economy pumped up by runaway land prices and Alice-in-Wonderland share valuations. The whole thing crashed in 1992 with a thud heard round the world.

Meanwhile, the Big Three U.S. auto makers narrowed the quality gap, U.S. PC makers left Japanese rivals in the dust, and Internet upstarts like Netscape Communications Corp. and Yahoo! thrilled both geeks and investors. Now, it's the Japanese who are looking hungrily at America's dominance of software design, microprocessors, and Internet innovations. "We envy you Americans very much," says Fumio Sato, Toshiba Corp.'s outgoing president.

Uh-oh, America. Watch out when Japanese executives start laying on the sugar. In fact, many Japanese companies are gathering strength for a new assault on U.S. markets. Their domestic economy expanded by a stunning 3% in the first quarter, although economists fear it may be flat for the rest of the year. The stock market has soared 50% from last July's low of 14,485, while the yen has weakened dramatically, to 108 or so from a low of 79 to the dollar in April, 1995.

Already, there are telltale signs that competition from Japan is heating up. On June

17, for instance, Sony Corp. announced its first home computer for the U.S. market. Japanese carmakers are paring the monthly lease payments on their key models to the bone. And American steelmakers and machine tool producers may face renewed pressure from their Japanese rivals: The Commerce Dept. recently pushed through duties on a Japanese sheet steel producer for allegedly selling its product below cost.

Nobody is predicting a replay of the 1980s, when Japanese companies blithely snatched market share

WATCH OUT FOR JAPAN (REDUX)

ECONOMY Japanese companies finally have a strong home economy helping them: In mid-June, the government announced that GDP expanded by a remarkable 3%.

STOCKS The Nikkei index is now above 22,000, up 50% over last year's low.

YEN After hitting a scary high of 79 to the dollar in April, 1995, the yen has stabilized at around 109, making Japanese export goods cheaper for foreign consumers.

PROFITS Manufacturers' earnings are up 20% in the fiscal year ended March 31.

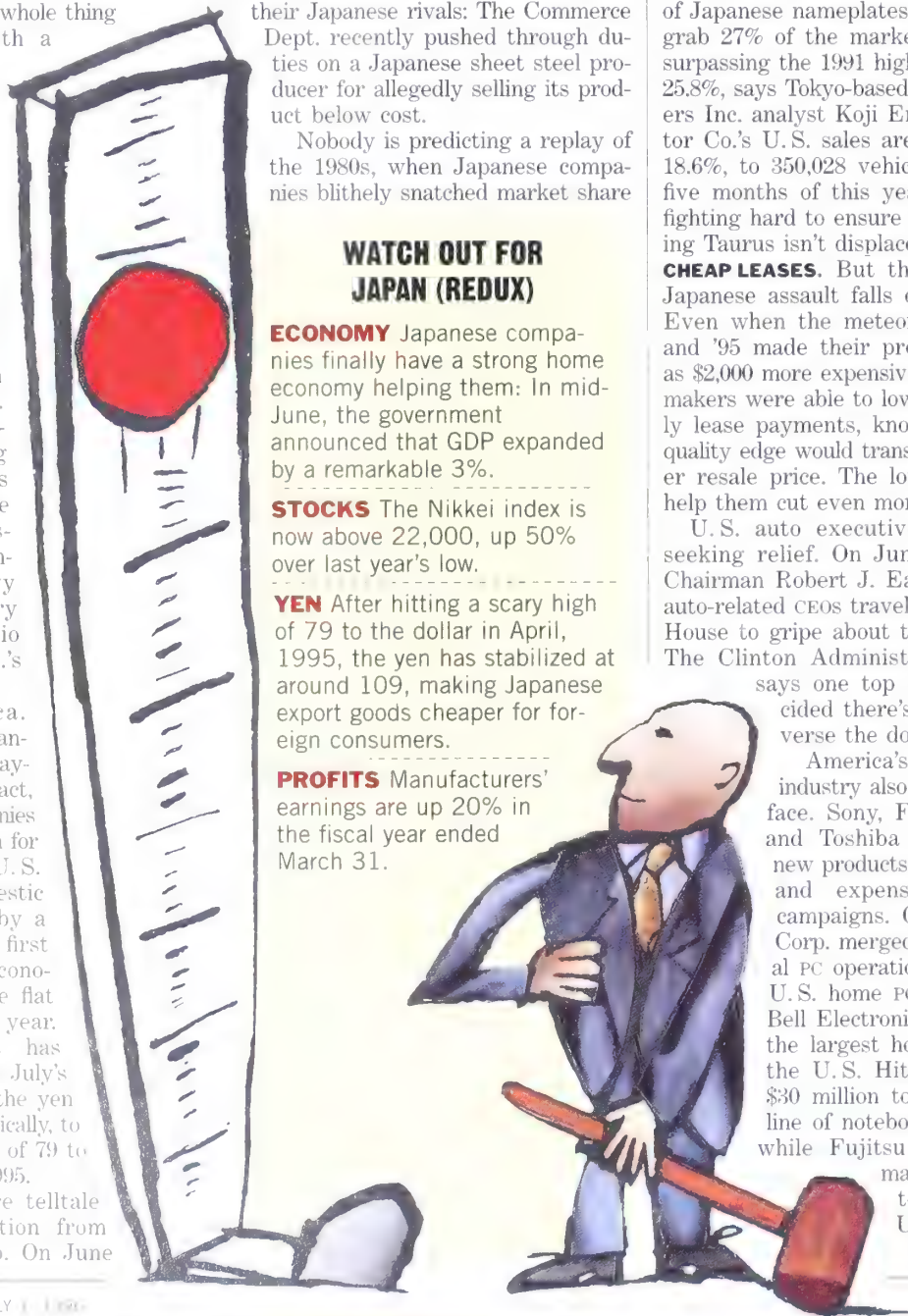
around the world by slashing prices—by dumping. But in the critical auto and computer markets, Japan Inc. is already making a big play to regain ground in the U.S. "The Japanese haven't been standing still," warns TRW Chairman Joseph T. Gorman.

The push has been on for some time in autos. With prices steady, the average break-even point of Japanese auto makers has been lowered to 90 yen or so to the dollar, figure auto analysts. The good news for consumers: When Toyota Motor Corp. introduces its redesigned Camry this fall, Lehman analyst Joseph Phillippi expects a \$1,500 markdown. That edge, plus the perceived quality of Japanese nameplates, could let Toyota grab 27% of the market by late 1996, surpassing the 1991 high-water mark of 25.8%, says Tokyo-based Lehman Brothers Inc. analyst Koji Endo. Honda Motor Co.'s U.S. sales are already up 18.6%, to 350,028 vehicles, in the first five months of this year, and Ford is fighting hard to ensure its market-leading Taurus isn't displaced by Accord.

CHEAP LEASES. But the brunt of the Japanese assault falls on auto leases. Even when the meteoric yen in 1989 and '95 made their products as much as \$2,000 more expensive, Japanese carmakers were able to lower their monthly lease payments, knowing that the quality edge would translate into a higher resale price. The lower yen should help them cut even more.

U.S. auto executives are already seeking relief. On June 12, Chrysler Chairman Robert J. Eaton and 30 other auto-related CEOs traveled to the White House to gripe about the rising dollar. The Clinton Administration, though, says one top official, has decided there's no need to reverse the dollar's climb.

America's star computer industry also has Japan in its face. Sony, Fujitsu, Hitachi and Toshiba have launched new products, big expansion and expensive market campaigns. On June 5, NEC Corp. merged its international PC operations with that of U.S. home PC giant Packard Bell Electronics Inc., creating the largest home PC outfit in the U.S. Hitachi will spend \$30 million to market a new line of notebooks in the U.S. while Fujitsu Ltd. has earmarked \$21 million to market a new U.S. PC offering. Japan has



ched product salvos before, only to a hasty retreat. This time, they st, it's different. "Everyone is vulnerable to a newcomer with muscle, nology, and ideas—we've got them gushes Hitachi PC President David cock. "I won't be satisfied until we No. 1" in notebook computers, says tsu PC Corp. President George rhardt.

till, behind all this bravado is a e of desperation. Japanese power- es such as Sony and Toshiba are tting on PCs becoming a key plat-

form in the convergence of consumer electronics with Internet gadgets. But without a credible position in the world's largest computer market, their investments won't matter much. To get there, Sony has jazzed up its two PC lines with advanced multimedia features for viewing videos, including pre-loaded clips from Sony movies. Priced between \$2,000 and \$3,000, Sony's PCs will win a beachhead in the high end, the company hopes.

It won't be a walk, though. U.S. auto and computer companies have never

been better positioned to fend off an assault from Japan. The PC makers, for example, have established strong brands of their own. There's a risk, too, that all the pricing adjustments and product offerings will merely shift market share from one Japanese rival to another. But for the first time in years, the U.S.-Japan rivalry seems ready to heat up in America. In many industries, that smug smile Americans have had for the last few years may be about to fade.

By Brian Bremner in Tokyo, with bureau reports

DODGE'S MINI-RAM TO THE RESCUE?

When red-hot Chrysler Corp. unveils a new product these days, Detroit pays attention. But its redesigned 1997-model Dodge Dakota truck, first shown publicly on June 19, is drawing more than the usual buzz. With this one, Motown is wondering whether Chrysler can jump-start the sluggish compact-pickup market—and steal some sales from Japan and its crosstown rivals in the process.

Right now, Detroit is pulling out all the stops to produce more trucks—and selling just about all of them it can produce. But contrary to the trend, the compact segment is down 10% so far this year. Manufacturers have slapped on hefty rebates, but consumers are still raving to the more powerful full-size models. "It's a function of price and value," says James K. Lust, president of Lust Chevrolet-Tuick-Geo Co. in Aberdeen, S.D. People don't want a small pickup when, for \$2,000 or \$2,500 more, they can buy a full-size."

RAWNY. Chrysler aims to change that mind-set. Its current, boxy version, the Dakota, trails the Ford Ranger, Chevrolet S-10, and Toyota Tacoma in U.S. sales, but the 1997 model boasts the brawny styling of Chrysler's wildly popular full-size Ram pickup. The 1997 Dakota is also wider and longer than rival models and is available with an optional V-8 engine. "It's a real truck, not a toy truck," says



THE '97 DAKOTA: It could rev up the compact-truck market

Bernard I. Robertson, Chrysler's general manager for Jeep/Truck Operations.

Japanese auto makers created the compact-pickup segment in the late 1960s with a series of inexpensive vehicles powered by four-cylinder engines. But a 25% tariff imposed on Japanese pickups by the U.S. government in the mid-1980s, coupled with a stronger yen, destroyed their price advantage. Ford Motor Co. and General Motors Corp. capitalized on the situation by updating their compact entries in 1993. After peaking at 1.2 million units in 1994, though,

compact sales have been in decline. That's partly because gas is cheap and partly because the aging population of truck buyers favors bigger, more solid vehicles.

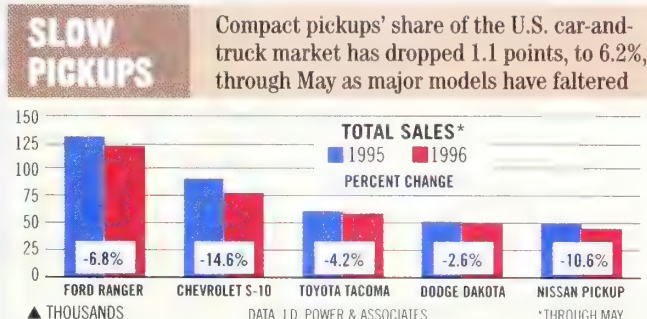
Chrysler is betting that the new Dakota will reverse the trend when it hits the showrooms this fall. Its styling borrows heavily from the Ram. The optional V-8 engine provides 230 horsepower, which dwarfs the output of the biggest V-6 engines offered by Ford and GM. The Dakota also has stan-

dard dual air bags and more space in the passenger compartment than its rivals. Chrysler won't divulge prices until August. But it hints that the base price won't rise much from the current model's \$11,580, with a fully loaded, extended-cab version likely to cost more than \$20,000.

If Chrysler's record is any guide, the new pickup will be a winner: Sales of the Ram are up 65% over last year. Chrysler's overall sales through May also are up 18.5% over last year, and it plans to hike total production by 12% in the third quarter vs. the same period in 1995.

"Chrysler is doing a better job of interpreting the customer's needs than any other auto maker right now," says Schroder Wertheim & Co. analyst John Casesa. And now that Chrysler is revving up the Dakota, the compact-truck market may be in for a smoother ride.

By Bill Vlasic
in Detroit



COMMENTARY

By Mike France

CORPORATE LITIGATION: PLAYING HARDBALL IS ONE THING..

In 1991, Exxon Corp. gave \$70 million to a coalition of seven seafood processors who lost business because of the Valdez oil spill. The company publicly boasted that it handed over the money out of the goodness of its heart—with no strings attached. In fact, though, it had confidentially struck an agreement with the processors that required them to give back any punitive damages they ultimately won.

On June 11, after learning of the true situation, the judge presiding over the case went ballistic. Exxon's lack of forthrightness, he said, meant that the jury charged with punishing the oil company for one of the worst environmental disasters in history heard corporate officers brag about the company's generosity to the seafood processors—but not how it extracted valuable concessions in return. "Exxon has acted as a Jekyll and Hyde, behaving laudably in public, and deplorably in private. The court is shocked and disappointed that Exxon has entered into such a repugnant agreement," wrote U.S. District Judge H. Russel Holland. He prohibited the seafood processors and Exxon from receiving any portion of the \$5 billion in punitive damages, a decision that stands to cost the company more than \$700 million. Exxon says Judge Holland's legal analysis is incorrect and is appealing the ruling. **"CHEATED CONSCIOUSLY."** Unfortunately, this is hardly an isolated instance of alleged litigation misconduct. Corporate foul play in high-stakes cases appears to be increasing. Last August, for example, a Georgia court fined DuPont Co. \$115 million for withholding key documents in a lawsuit brought by shrub and tree growers alleging that the fungicide Benlate injured their crops. Wrote U.S. District Judge J.

Robert Elliot: "DuPont cheated. And it cheated consciously, deliberately and with purpose." The company denies the charges and is appealing the ruling. But in April, three contract workers made fresh accusations that DuPont concealed negative Benlate test results, which the company also denies.

The list of companies that have received similar court



censures in recent years goes on and on: General Motors, Suzuki Motor, and pharmaceuticals maker Fisons, just to name a few. Of course, destroying evidence, striking secret deals, and stonewalling opponents aren't new tactics in the world of hardball corporate litigation. But it is difficult to recall a time when so many respectable companies have been hit with court sanctions. The problem has become so acute that courts in New Mexico and New Hampshire last year created tough new case law punishing litigation misconduct.

It's not hard to figure out how things got to be this way. Tens of millions of dollars can ride on an indi-

vidual lawsuit. Frustrated by tort laws they see as tilted against them, large companies can be tempted to break the rules. And many attorneys no longer have the courage to say no, afraid of losing key clients in the face of unprecedented competitive pressure. "Lawyers used to be pillars of the community, upholding centrist values. Today, they see their job as pushing the envelope of what is legal

and illegal," says Philip K. Howard, author *The Death of Common Sense*, a critique of the legal profession.

INEXCUSABLE. Of course, many of the complaints that large corporations have against America's legal system are valid, and some business attorneys complain that judges have sanctioned them inappropriately. But the recent trial tactics of Exxon, DuPont and others are inexcusable. No one—and no company—should hold itself above the law. And their obtuseness may yet backfire. By refusing to play by the rules, these companies have undercut their moral authority to criticize the U.S. tort system. If these companies and others expect popular support in their legitimate battle for legal reform, they are going to have to start behaving

better than the plaintiffs' lawyer they so frequently criticize. And so far, that's not happening.

For their part, judges must do a better job of policing the high-stake cases that land on their dockets. One of the main reasons corporate attorneys are willing to take ethical risks is that judges have traditionally been reluctant to hand out stiff punishments for seemingly minor offenses such as discovery abuse. Litigation misconduct will only stop when the courts ensure that it doesn't pay off. Judge Holland's decision is a good start.

France is *BUSINESS WEEK's* Legal Affairs editor.

OW NBC WON HE TRIPLE CROWN

e NBA, Olympic trials, and U.S. Open pay off

The weekend of June 15, NBC Sports did to the competition what *Seinfeld* has been doing for years: Crushed it. NBC had Michael Jordan, Carl Lewis, and Greg Norman highlighting NBA finals, Olympic trials, and U.S. Open, while ABC featured European men's gymnastics, CBS offered elderly heavyweight Larry Holmes leaning into new punches, and Fox had baseball's *Game of the Week*.

General Electric Co.'s NBC Inc. gained not more than bragging rights. Its five-year, \$715 million National Basketball Assn. fee, quadruple what CBS Inc. paid for the 1986-1990 NBA seasons, is going off. The Chicago Bulls-Seattle SuperSonics series was the second-most-watched finals in NBA history. The sixth hour Sunday night garnered an 18.8 Nielsen rating, making it the third-highest-rated show of the season after *E.R.*

Seinfeld. Media analysts figure the network broke even by the Friday night broadcast and netted a \$10 million profit on Sunday's game. "All the accounts at NBC have severe hangovers after a wild night of partying," cracks NBC Sports President Dick Ebersol.

The rest of the weekend was almost as much fun for the bean-counters. NBC's marathon 12 hours of coverage of the U.S. Open on Saturday and Sunday earned a 4.7 rating for both days, a solid performance for daytime programming. Saturday's track and field championship garnered a 4.9 rating as NBC began airing the Atlanta Olympic Games. Not the greatest [prime time rating], but in the cost analysis, it's barely fine," says Peter Chrisanopoulos, president of broadcast programming at Ogilvey & Mather Worldwide and ABC's former research head. NBC capped its sports marathon by signing a six-year contract on June 18 with sportscaster commentator Bob Costas.

EBERSOL'S OLYMPIAN BET. Years of losing are behind NBC's sports push. In 1989, when Ebersol, a former independent TV producer, joined NBC Sports, the cupboard was bare. He was forced to dream up such events as the *Lee Trevino One-handed Challenge*, where the golfing at would compete one-handed. It presented an idea to corner all the crown jewels in sports," says

Ebersol. Soon afterward, he grabbed the NBA games from CBS, which instead spent \$1.06 billion on baseball—and ended up with a \$500 million loss.

Ebersol made the right bet. "CBS now drools with envy about NBC's basketball deal," says Paul Schulman, a media-buying consultant. "There should be a statue of Dick Ebersol at Rockefeller Center." NBC has all but commissioned one: In May, the network signed Ebersol to a contract through 2004, the longest term ever given to an executive of NBC—or GE.

The agreement gives Ebersol plenty of time to play out his biggest gamble—the right to broadcast all five of the Olympics from 2000 through 2008. NBC went after this prize last August, when it made a \$1.27 billion offer for the 2000 Summer Games in Sydney and the 2002 Winter Games in Salt Lake City. Four months later, Ebersol struck again, sealing up the



AHEAD OF THE PACK: Profits have followed strong ratings

next three Olympics for \$2.3 billion.

That's a lot of money, given NBC's rocky Olympic history. The network paid \$87 million for the 1980 Moscow Olympics, only to fall victim to President Carter's boycott. It lost money in 1988 at Seoul and in 1992 at Barcelona—and in both years its time-delayed broadcasts got dismal U.S. ratings. Seems like a poor basis for spending \$456 million for the two-week Atlanta games—\$56 million more than News Corp.'s Fox Broadcasting pays for an entire season of pro football.

"Everyone wondered, when the Atlanta numbers were announced, would they break even?" says Chrisanthopoulos.

The answer, insists Ebersol, is yes. "All of our sports programs are profitable," he says. In fact, the Atlanta games could break the Olympic jinx because they can be broadcast live during prime time. And the next Olympics, the 2000 Sydney Summer Games, will take place from Sept. 16 to Oct. 1—the exact start of the fall TV season. "What network would have the nerve to put new original programming against the Olympics?" asks Schulman. "NBC will have two weeks to promote its fall prime-time lineup." That's a move shrewd enough to make Kramer proud.

By Michael Goldstein
in New York

GOING FOR THE GOLD

NBC's sports broadcasting lineup

OLYMPICS Summer games, 1996–2008; winter games, 2002–2006

FOOTBALL NFL play through 1997; Notre Dame games through 2000

GOLF Professional Golfers Assn. tour

TENNIS Wimbledon and French Open through 1999 and 1997, respectively; U.S. Open through 2000

BASKETBALL NBA through 1998

BASEBALL Post-season Major League Baseball through 2000

HORSE RACING Breeder's Cup through 2000

DATA: COMPANY REPORTS

DEALS

LOTUS' POSITION: ALONE FOR NOW

Netscape says no to an Internet server alliance

In early June, a group of Lotus Development Corp. executives made a secret trip to Mountain View, Calif., to visit Netscape Corp., maker of the No. 1 Web browser. Netscape co-founder Marc L. Andreessen had expressed interest in a new Net version of Notes, Lotus' popular software program that helps workers collaborate. The Lotus execs saw their chance: They just had to persuade Netscape to adopt elements of Notes, rather than spend months building a competing technology.

The issue was more than academic for IBM, which paid \$3.5 billion for Lotus last July. Big Blue has spent the past year defending its acquisition against criticism that the Internet will soon undercut Notes by providing a cheaper alternative. An endorsement by Netscape would help quell the critics. Most important, an alliance between Netscape and Lotus might be both companies' best hope for fending off Microsoft Corp.'s advances onto the Internet.

TIME LIMIT. But the best-laid plans... Andreessen was impressed, but not enough to drop Netscape's efforts. It had just paid \$172 million for Collabra Software Inc., a maker of Notes-like programs. A less ambitious partnership was explored, involving joint efforts such as uniting Notes' E-mail with Netscape's Web browser. But no go.

Lotus insiders say the two sides just couldn't agree on details in time for a press conference to unveil the new Notes version. They were still negotiating on the eve of the announcement, but on June 19, Lotus execs

took the stage at a New York press conference alone to unveil Domino, a new Web-friendly line of Notes software. Instead of a Netscape deal, they unveiled a new Internet version of Notes. Analysts say Domino, due at yearend, is top-notch. Says David Marshak, a consultant with Patricia Seybold Group: "This will give Microsoft a run for its money." And maybe Netscape, too.

By Amy Cortese in New York

COMMENTARY

By Stan Crock

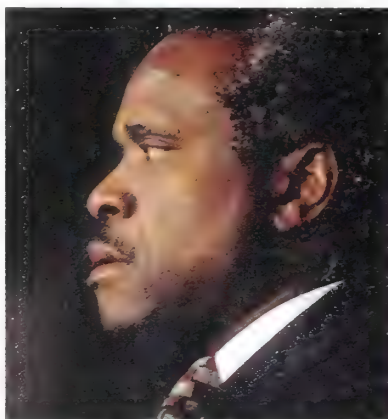
WHAT IF A SUPREME COURT JUSTICE PREJUDGES?

Four centuries ago, British jurist Lord Coke wrote: "No man should be a judge of his own case." It's a simple notion: Judges should recuse themselves when their impartiality is in question. But some Supreme Court justices just don't get it.

The latest example is Justice Clarence Thomas. In a June 10 opinion upholding Lockheed Martin Corp.'s early-retirement plan, he cut back on the reach of a 1986 law that requires companies to give workers pension credit for service past retirement age. Problem was, that was the same stance Thomas had taken in 1988 in a dispute with the Internal Revenue Service when he was chairman of the Equal Employment Opportunity Commission. The IRS, which backed retroactivity, won the fight, transferring some \$3 billion from corporate coffers into workers' wallets.

Why is Thomas' past involvement a problem? A 1974 federal law disqualifies judges who, while serving in government, have "expressed an opinion concerning the merits" of a case. "You don't want a judge sitting on a case where he has taken a position," says Stephen Gillers, a legal-ethics expert at New York University Law School. Justices currently decide for themselves whether to sit on cases. But to preserve the court's integrity, that must change.

Congress has tightened the rules for judges before, notably after a flap involving then-Associate Justice William H. Rehnquist. As a Justice Dept. official before joining the bench, Rehnquist defended Army surveillance of domestic dissidents. Then in 1972, he provided the swing vote to toss out a suit challenging the operation. In the ensuing controversy,



THOMAS: His earlier stance cried out for recusal in a Lockheed case

Congress toughened its rules.

Too bad Thomas didn't heed the changes. Consider what he said on Jan. 26, 1988. Moments before an EEOC meeting, the IRS had asked the agency to delay adoption of a final pension rule the IRS opposed. According to a transcript, Thomas said, "We think that substantively we are absolutely correct."

Thomas had already shown his views on the issue in other ways. A EEOC chief, he failed for years to revoke a rule allowing companies to freeze pension benefits for employee who worked past retirement age. His foot-dragging so angered Judge Harold H. Greene that Greene questioned Thomas' truthfulness and accused the EEOC of "utter administrative capriciousness."

Thomas declines to comment. But Clint Bolick, litigation director at the conservative Institute for Justice, says: "I'm confident that if he had perceived this issue as a substantive legal matter, he would have recused himself." And Thomas no doubt would argue that he had an open mind in considering the issues anew.

THE CURE. Still, it was too easy to predict how Thomas would vote, and that's the problem.

Jeffrey W. Stempel, a professor at Florida State University College of Law, suggests a sensible remedy: When justices don't recuse themselves, allow either side in a case to appeal to the full court and require a written decision. An airing of the issue might force the court to focus on its institutional interest in protecting its integrity. Even Lord Coke would approve.

Crock covers defense for **BUSINESS WEEK**.



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EDITED BY KELLEY HOLLAND

THE BAILOUT BUCKS FLOW BACK

WHAT GOES AROUND, COMES around—at least this time. Just over a year after a Washington-sponsored bailout package rescued Mexico from financial default, Mexico is repaying \$4.7 billion of the \$12.5 billion it borrowed from the U.S. Treasury, thanks to bond issues. The U.S. Treasury had been pushing Mexico to prepay some of the debt it took on in January, 1995, and purposely set interest rates high on the rescue package—around 10.2%—to encourage such moves. Mexico has made two other prepayments but still owes Washington \$5.8 billion, even after the latest payment. One reason Treasury is

in a hurry: The Clinton Administration would like to put the politically unpopular bailout behind it by having Mexico repay the bulk of the rest of its debt by the first week in November.

A SECURITIES BILL CONGRESS CAN LOVE

NO GRIDLOCK HERE: NEW securities legislation is sailing through Congress. On June 18, the House passed a bipartisan bill intended to streamline regulation of small companies and mutual funds. The bill would cut duplicative state regulation and have federal, not state, rules cover mutual-fund sales and securities offerings from companies with more than \$10 million in assets. States will continue to police securities fraud. The Senate Banking Committee approved its version of the bill on June 19. A final compromise version is expected to get President Clinton's signature this fall.

DEC GETS ITS CHIP OFF THE BLOCK

AT LAST. AFTER STRUGGLING for years to find a computer maker willing to adopt its high-performance Alpha chip, Digital Equipment on June 18 announced that Samsung Semiconductors will license Alpha. The deal anticipates a boom in demand for semiconductors to run Microsoft's Windows NT operating system. Samsung plans to make Alpha chips in Korea and then use them in servers and high-end workstations sold by PC maker AST Research, in which Samsung owns a stake. One potential glitch for DEC: Analysts fear Samsung may drive down the price of Alpha chips—which could hurt DEC's own chipmaking.

HEADLINER: WILLIAM JOHNSON

A DIET DOCTOR IN THE HOUSE

William Johnson, who built his career on tuna fish and pet food, is about to get a crash course in dieting. Before becoming the new president and chief operating officer at H.J. Heinz, Johnson, 47, cut costs and boosted earnings at the company's pet food and Star-Kist units from his base in Cincinnati.

Now, moving to Pittsburgh, where he's heir apparent to Chairman Anthony O'Reilly, Johnson must turn similar tricks with Weight Watchers, Heinz's laggard division. O'Reilly says Johnson's chances of replacing him as CEO in three years hinge largely on

the performance of Heinz stock—and squeezing dollars from Weight Watchers will be key. Yet even

Heinz announced record earnings June 18 of \$66 million, it said frozen-entrée sales were flat. Johnson, the son of ex-Cincinnati Bengals coach Bill "Tiger" Johnson,

clearly speaks the same language as O'Reilly, a former rugby star. Both talk about "putting points on the board." Johnson made Morris the cat purr. Now he must get Weight Watchers up to par.

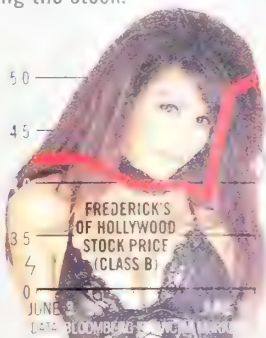
By Stephen Baker



CLOSING BELL

OOH LA-LA

Frederick's of Hollywood has finally tantalized the market. Since hitting a high of 6 1/2 a share last summer, Frederick's B stock had been mostly weak until management announced on June 14 that the company may be for sale. Shares jumped 29% in two trading days, to close at 5 on June 18. A trust that owns 50% of Frederick's needs to sell to raise cash to pay taxes, and the company's poor performance was depressing the stock.



BIG BLUE HEADACHES IN ARGENTINA

TROUBLE IN ARGENTINA: FOR the past year, a judge there has been looking into allegations that IBM employees and the company's joint-venture partners paid kickbacks to win a \$249 million contract for work at state-owned Banco de la Nación. And on June 18, IBM's woes increased. In a different inquiry, another Argentine judge seized documents at IBM's Buenos Aires headquarters in connection with a \$525 million deal with the federal revenue department to process pension payments for four years. IBM says it believes the price of the contract is fair.

FEWER CHOICES IN THE TOFU AISLE

HOLY GRANOLA! THE \$9 billion natural-foods industry is rapidly consolidating with

the June 18 bid by Anaheim (Calif.)-based Whole Foods Market to buy Fresh Fields, a Rockville (Md.) chain with \$135 million. Whole Foods No. 1 in natural-food sales with \$496 million in revenues, says it has a deal with owners of 69% of Fresh Fields stock to complete the deal. The deal is expected to close in September. Whole Foods already owns Boston's Bread & Circus and Los Angeles' Mrs. Gooch's Natural Foods Markets.

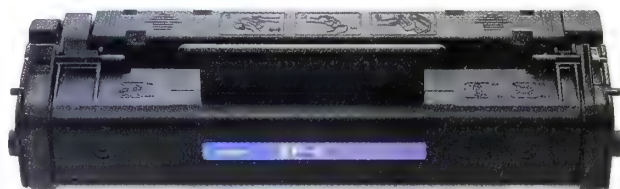
ET CETERA...

- Tele-Communications Inc. to spin off its direct-broadcast satellite unit.
- Whitewater: Clinton adviser Bruce Lindsey was named in an unindicted co-conspiracy.
- Navistar International cutting 3,000 jobs at its tire plant in Springfield, Ohio.
- Tenneco is selling its energy division to El Paso Energy in a \$4 billion deal.

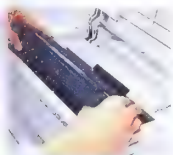


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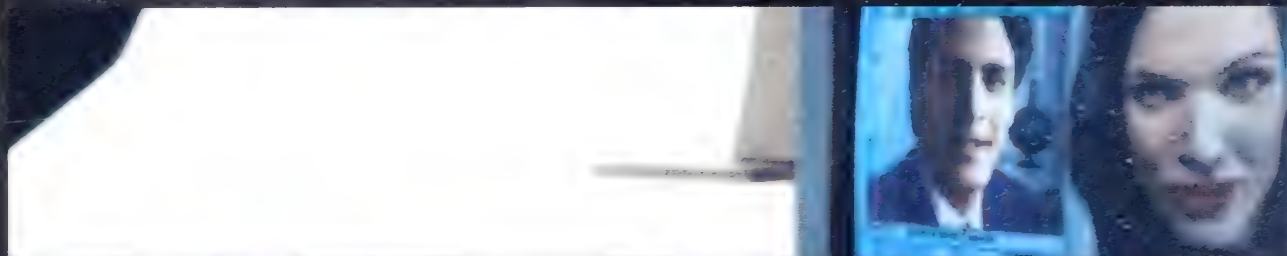
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EDITED BY OWEN ULLMANN

WANTED: A NEW FLIGHT PLAN FOR THE FAA

On June 18, Transportation Secretary Federico F. Peña asked Congress to do what critics have demanded for years: end the Federal Aviation Administration's dual—and mes conflicting—missions of promoting the airline industry and policing safety. Now safety is the only goal.

FAA Administrator David R. Hinson has shown he's with the program. He grounded ValuJet Airlines Inc. in the wake of a 11 crash in the Florida Everglades, sacked top safety official Anthony J. Broderick, and vowed to modernize an agency even FAA insiders concede can't keep up with a rapidly evolving, deregulated industry. End of story? No, it's just the beginning—no guarantee of a happy ending. Reining any federal bureaucracy is tough. But in the case of the 48,000-employee FAA, the task is especially daunting. Airlines won't surrender their clout without a fight. And Congress can't agree on an overhaul. Some lawyers want to make the FAA an independent agency; others want to spin off air-traffic control into a quasiprivate company.

When there's the secretive FAA management, its military mindset, industry sympathies, resistance to change give critics fits. For example, the FAA has resisted numerous safety proposals by the National Transportation Safety Board, saying the changes would be too costly for airline and aircraft makers. "I don't think just one individual being fired or let go is going to change the culture," argues retiring Senator William S. Cohen (Maine), whose subcommittee oversees the FAA.

For outsiders such as Cohen, the FAA's shortcomings have been obvious. The nation's air-traffic-control computers routinely break down. FAA officials rely heavily on industry views in making crucial safety decisions. And the agency has a "tombstone mentality" of acting only after a tragedy, as in the shakeup triggered by the 110 deaths in the ValuJet crash. "The agency

is often called upon to reform itself," says aviation-economics expert Darryl Jenkins of George Washington University. "But it can't do it. It's part of the problem."

That's why the House agreed last March to make the FAA an independent agency headed by a CEO and funded by the 10% passenger-ticket tax that expired on Jan. 1. The Senate is working on its own bill. Senate Commerce Committee Chairman John McCain (R-Ariz.) favors an FAA modeled after the FBI, which is independent but reports to the Justice Dept.

He also wants to form a management advisory council and fund the agency with industry user fees rather than ticket taxes.

The Clinton Administration came up with the boldest plan—a government corporation to take over air-traffic control and a narrow FAA mission to oversee safety. But the GOP buried it. So the Administration now backs McCain's approach.

COSMETICS. While pols struggle to find a bipartisan fix and investigators look into possible criminal wrongdoing at the agency (page 4), many FAA insiders think there'll be more blood-letting, with Hinson—an ex-airline CEO—the next possible casualty. But that would be just more cosmetics covering the fundamental flaws, staffers say. Contends one FAA inspector: "We need to change top management, middle management, and the entire corporate culture."

Congress and the White House agree, but can't seem to solve the problem. And the airlines are sure to mount a campaign to protect their influence. "This is a safe system," says a spokesman for the industry's Air Transport Assn. "Let's get the facts before we make a decision driven by emotions." Given the agency's 38-year history of resistance to change, the battle to reinvent the FAA is sure to be long and frustrating.

By Christina Del Valle and Douglas Harbrecht, with Willy Stern in New York



HINSON: *The next to go?*

CAPITAL WRAPUP

COUP FOR CHIRAC

French President Jacques Chirac will make economic summit history when he hosts the Group of Seven's annual meeting in Lyon on June 27-29. Chirac has invited the heads of the N., International Monetary Fund, World Bank, and World Trade Organization to attend the G-7 for the first time to press France's case for more multilateral cooperation. That could be a slap at the U.S., which has been criticized by allies for increasingly going its own way in foreign affairs.

REICH'S COMP BANK

► Labor Secretary Robert B. Reich has ordered his staff to brainstorm ideas to counter proposed GOP reforms to the Fair Labor Standards Act. Republicans want to give employers more freedom to adopt work schedules that don't fit the standard 40-hour week. Reich's counter: a "comp time bank" to let workers store unpaid overtime, overriding employers' limits on how long comp time can be saved. "We want to have a worker-friendly response," says a Labor aide.

NEWT'S WAR GAMES

► Newt Gingrich is calling in the military to quell rebellions by conservative Republican freshmen. The Speaker has asked three officers on loan from the Pentagon to help assess strategy and tactics for maintaining party unity. The most recent brush with disaster came on June 13 when a mutiny by 15 frosh nearly sank Gingrich's 1997 budget blueprint. The Georgian, a former Army brat who never served, is an avid student of military history.



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EUROPE

PILING INTO CENTRAL EUROPE

Stability and big economic gains are luring investors to Poland, Hungary, and the Czech Republic

It has been a quiet revolution. While the turmoil in Russia has held the world's attention for months, another part of the old Soviet bloc has been reshaping itself. Thanks to a combination of political stability, an able labor force, and consistent economic reform, Poland, Hungary, and the Czech Republic are managing to outshine other countries in Eastern Europe and the former Soviet Union.

Inflation has tapered off, once-gyrating currencies are now stable, output is rising at a brisk pace, and unemployment has leveled off. Poland's gross domestic product increased by 7% in 1995, rivaling Taiwan's 6% and Indonesia's 5.1%. This year, Poland and the Czech Republic are forecast to expand by 5.5%, placing them among Europe's most robust economies.

Such growth is producing a prosperity that no one wants to endanger. Thus, even the former communists who rule in Poland and Hungary are dedicated to promoting the flow of investment. And Milos Zeman, the Czech Social Democrat who did surprisingly well against free-marketer Vaclav Klaus in the recent election, is emphatic in his defense of the fundamental direction of the economy. **INDUSTRIAL MIGHT.** The country's

this stability is a wave of foreign investment in everything from auto assembly to retailing. Direct foreign investment in Poland, Hungary, and the Czech Republic doubled in 1995, bringing the total since 1990 to \$23.5 billion. Cumulative investment is expected to jump an additional 20%, to \$30.4 billion by yearend. Says Dan Lubash, head of European emerging-markets research at Merrill Lynch & Co.: "Give these countries two more years, and they'll be like the Asian tigers."

That kind of optimism is finally attracting investors from Asia who had

long viewed the region as too risky. In January, Matsushita Electric Industrial Co. said it would build a \$66 million TV plant in the Czech Republic. Daewoo Motor has pledged \$1.47 billion for two plants to assemble cars and vans in Poland. In March, Sony Corp. chose Hungary for its newest European factory, a \$20.4 million plant that will make CD players, stereos, and color TVs for sale throughout Europe. "These countries have become dependable," says Jack Schmuckli, chairman of European operations at Sony. "They will keep our European manufacturing competitive."

Certainly, problems remain. Central Europe must still repair the damage left by four decades of mismanagement—from bloated pension systems to inefficient factories in need of overhaul. Former Communist Party bureaucrats at state-owned companies in Poland have managed to bog down privatization: In recent weeks, the high-profile bankers and policymakers who disagreed with a controversial plan to consolidate banks were fired—a blatant act of interference.

Despite these irritations, more and more global companies are convinced they can earn a healthy return on their investments. Productivity in the region is rising fast enough to outweigh wage increases. For example, Creditanstalt-Bankverein calculates that unit labor costs in Hungary in dollar terms will



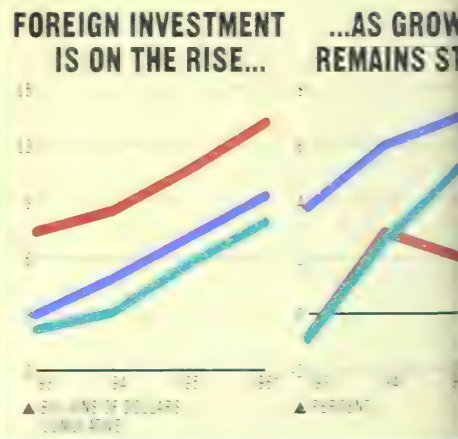
drop 10% in 1996, even as wages paid forints are increasing. To attract investors and prepare for membership in the European Union, Czech, Polish, and Hungarian leaders are steadily aligning tax, labor, investment, and banking rules with those in the West and relinquishing controls on hard currency.

The new rules are making it much easier for corporations to raise cash. ING Bank and Citibank have issued corporate bonds and commercial paper

Turning the Corner in Central Europe

■ POLAND
■ HUNGARY
■ CZECH REPUBLIC

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A Flood of Foreign Investment

ADAM OPEL Plans to build a \$340 million car plant in southern Poland

DAEWOO MOTOR Edged out General Motors to buy 70% of Poland's FSO auto maker for \$440 million

IBM Plans to spend \$40 million to triple the capacity of its disk-drive plant in Hungary

MATSUSHITA Announced a new \$66 million TV plant in the Czech Republic

GE CAPITAL Bought a 27.5% stake in Budapest Bank for \$39.9 million

AGIP, CONOCO, ROYAL DUTCH/SHELL Bought 49% of Czech Refining for \$149 million; pledged an additional \$480 million over five years

DATA: BUSINESS WEEK

Hungary's sixth-largest. The EBRD wants a 15% return on equity, similar to what a healthy Western bank brings in. Bela Singlovics, chief executive of Budapest Bank, is keen on pushing the auto loans and credit cards, which are now found in only 8% of Hungarian wallets. "With GE, we can be a major player in consumer finance," he says.

The region's consumers are now on a lot of radar screens. Poland, for example, has seen per capita GDP rise by more than \$2,000 in six years, to about \$3,500. A group of U.S. and Canadian investors wants to set up a network of U.S.-style shopping malls, starting in Hungary on a former Soviet army base. France's E. LeClerc opened a hypermarket, a vast French-style emporium, in Warsaw in November and plans an additional 50 in Poland, aiming to share a good portion of the \$34 the average Pole spends on groceries each month.

CABBAGE AND SAUSAGE. Judging from the crowd one Thursday at 6:30 p.m., it looks like an easy task. Some 2,000 shoppers jam the vast, high-ceilinged hypermarket in József, the heart of a working-class borough north of downtown Warsaw. Polish cabbage rests alongside Argentinian oranges and fresh fish filets, while four tall shelves stock sausages in every shape, size, and flavor. A few meters away are auto and office supplies, videos, and vacuum cleaners. About 90% of the 15,000 products for sale are Polish.

But it's the heavy-duty manufacturing investments that are reshaping the industrial map. Siemens was among the first to move to a facility across the Czech border, where rows of women hand-weave multicolored wiring destined for BMW cars. Inexpensive labor often gives these countries an edge over eastern Germany, where employers must pay nearly the same high wages and taxes as in western Germany.

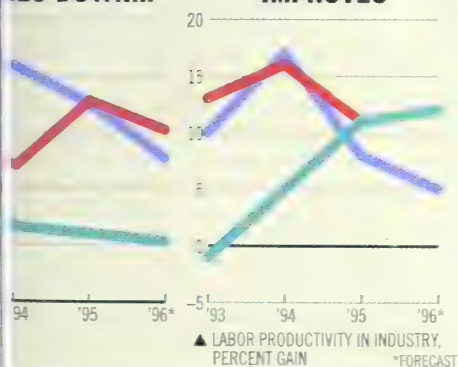
Besides exporting cheap industrial

ing more than \$2 billion since the start of 1995. In April, Standard & Poor's Corp. rated Poland's debt investment-grade, a status the Czechs have enjoyed since 1993. "There is now a tier for investors to target," says Anne Gahler, an economist at J.P. Morgan & Co. Hungary's stock market surged 73% in dollar terms this year, while Poland's is up 44%. One of the biggest surprises for investors has been how much local talent

there is to bankroll. Take Imre Somody, who a decade ago hit upon the idea of a vitamin-C tablet that dissolves in water to become a fizzy drink. The state drugmaker where he worked rejected it, so in 1988, Somody and a few colleagues founded Pharmavit. They created Hungary's best-known brand: Plusssz vitamins. Pharmavit also makes generic drugs at its two modern plants outside Budapest. By 1995, sales had soared fivefold, to about \$42 million. Bristol-Myers Squibb Co. recently paid \$110 million for Pharmavit and put Somody in charge of all products in Hungary, from cancer drugs to Clairol hair care.

Other outsiders see big potential in creating world-class financial services for Central Europe's consumers. GE Capital Corp. is moving into the region as part of its global expansion. After buying a small Polish bank last year, GE Capital teamed up with the European Bank for Reconstruction & Development (EBRD) in December to pay \$87 million for a 60% stake in Budapest Bank,

FLATION DOWN... ...AND PRODUCTIVITY IMPROVES



goods, Central Europe is turning into a large market. To meet the demand, Goodyear Tire & Rubber Co. last year offered \$115 million for a controlling stake in tiremaker TC Debica in southeastern Poland. Goodyear says it has already boosted daily output by 25% to 30%. While demand is growing by no more than 3% in Western Europe, it is surging by at least 15% in Eastern markets. Poland is the place to be "if you're looking to where you can have an overnight market," says Sylvain G. Valensi, vice-president in charge of Goodyear Europe.

"BACKBONE." Cars are probably Central Europe's hottest spot. That's why Daewoo Motor pushed so hard to take a 70% stake in Poland's state-owned carmaker, FSO, last November, edging out General Motors. Kim Woo Choong, Daewoo Corp.'s chairman, aims to export \$1.5 billion worth of cars and car parts from Poland within three years. GM's Adam Opel will build a \$340 million factory in southwestern Poland to make a low-cost version of the family-size Astra.

The billions invested by the likes of

Demand is growing slowly in Western Europe, but it's surging in Eastern markets

Opel nourish new supply networks throughout the region. By the end of the decade, GM aims to derive \$1 billion worth of parts from Central Europe every year. Volkswagen's presence at Skoda has led to 46 auto-parts joint ventures and 28 new factories. Skoda buys parts from a total of 234 Czech companies. "The strength of the Czech supply industry is the backbone of our success," says Volkhard Köhler, Skoda's vice-chairman and chief financial officer.

Such dynamism will guarantee Central Europe's growth for the next few years. It will be hard-pressed to match Southeast Asia's scorching rates of 8% to 10%. But Poland, Hungary, and the Czech Republic are nonetheless pulling away from the frontier capitalism of their region and offering a safe zone for investors. As global investors contemplate where to spend their dollars, marks, yen, and won, Central Europe is a more competitive choice than ever.

By Karen Lowry Miller in Prague, with Peggy Simpson in Warsaw and Zachary Schiller in Cleveland

GERMANY

JUST WHEN LUFTHANSA WAS GAINING ALTITUDE...

More competition and overexpansion rob it of hard-won gain

Jürgen Weber wasted no time tackling Lufthansa's problems after taking over as chief executive of the loss-plagued airline in 1991. His strategy of freezing pay, dumping unprofitable routes, and cutting staff soon had analysts rushing to put Lufthansa high on their buy lists. Last year the carrier had record profits of nearly \$500 million on sales of \$13 billion.

But now Weber is fighting to preserve those gains, just as Europe's airlines are preparing for the ferocious competition that deregulation will unleash after Apr. 1, 1997. A June 17 German newspaper report that Lufthansa suffered a \$132 million operating loss in the first five months of the year pushed the stock down 8%, to \$143.20. Lufthansa would only acknowledge that "traffic figures and results are below target."

The going has certainly been a lot tougher. Lufthansa's key Düsseldorf hub, damaged by fire in April, is still not back in full operation. The strong German mark and the impact of Germany's mini-recession dragged cargo operations into a first-quarter loss of \$13 million and has depressed passenger traffic. The price of aviation fuel is up 16% so far this year.

FRENCH HANDOUTS. Lufthansa is also getting hit by the new world of cut-throat fare competition in Europe. One culprit, according to a complaint to the European Union by Lufthansa, KLM Royal Dutch Airlines, and Scandinavian Airlines System, is state-owned Air France. The Germans, Dutch, and Scandinavians charge the French carrier with using billions in taxpayer handouts to bankroll predatory pricing. An example cited is the route between Hannover and Marseilles, where a recent Air France fare was just \$113 round-trip, vs. \$207 for the cheapest competitor. An Air France official ripostes: "We have never been the leader [in fare-cutting]."

Lufthansa must also deal with woes

of its own making. Since January, for example, the carrier has added enough new flights to boost passenger capacity by nearly 5%, while traffic has increased only 2%.

Weber is acting fast to keep profits for the full year at their 1995 levels. In February, he imposed a hiring freeze. Now he's looking for new spending cuts as part of a five-year effort to slash \$660 million, or about one-fourth, from fixed costs. The airline also has sought new strengths. Cooperation with United Airlines, which feeds its American customers into Lufthansa's system, added an estimated \$65 million to the German carrier's bottom line last year. Wider cooperation with UAL Corp.



LUFTHANSA: Looking to United for more help

which has been approved by regulators, could raise that number to \$10 million next year.

But Lufthansa does not have a monopoly on strategic alliances. If British Airways PLC's planned cooperation with American Airlines Inc. clears regulatory hurdles, Weber might find himself running a lot harder just to stand still. As with full-blown deregulation fast approaching, says Frankfurt-based Solomon Brothers Inc. analyst Ralf C. Cullen, Lufthansa "still has to show that it can survive in a Pan-European environment." Lufthansa is a microcosm of Germany itself: struggling to be globally competitive while saddled with high wages, short working weeks, and bloated welfare costs. Problems like that take a lot of fixing.

By John Templeman in Bonn



STEERING CLEAR: Approvals of foreign investments are down nearly 50% from a year ago

growth. Investment figures overstate the money actually coming into the country. Of the \$22 billion, less than 20% has been disbursed, and investment approvals up to the end of May fell 48% from a year earlier, to just \$1.6 billion.

Vietnam could fall victim to a classic trap of reaping the easy gains of a newly opening economy without putting the fundamentals in place for the next stage of growth. The trade deficit is surging, and the country needs to invest massively to upgrade its tattered infrastructure. Soviet-style methods of running the economy also need to be changed.

Vietnam's financial sector is particularly ill-equipped to deal with the needs of sustained growth. The government has plans to raise about \$20 billion domestically—roughly equal to the country's current GDP—in the next five years. In a country where cashing a check is practically impossible, most experts think that goal is pie-in-the-sky.

Privatization could raise some funds, but so far the program has gotten off to a glacial start. The government has only partially sold off six state-owned companies by issuing shares that have raised less than \$15 million since the program was launched in 1992. Meanwhile, few of Vietnam's 6,000 state-owned companies would survive without preferential access to land and credit, not to mention the subsidies they receive. Two star state-owned companies, Vietnam Airlines and Vietnam Posts & Telecommunications, owe their success more to their monopoly status than to any management savvy.

Instead of restrictions, what the country needs is "aggressive reforms," World Bank President James Wolfensohn said during a visit to Hanoi in May. No country has ever achieved rapid industrialization on the back of the state sector, as Vietnam's hardliners would like to do. That's why the Party Congress could

be such a defining moment for Vietnam. If the leadership reasserts a dominant role over the economy, rather than spurring it to new levels, Vietnam is one tiger whose roar may never be heard.

By Frederik Balfour in Hanoi, with Joyce Barnathan in Hong Kong

ETNAM

REFORM ALIVE IN VIETNAM?

consolidate power, Hanoi is reining in the private sector

When Vietnamese government officials paid a visit to the Ho Chi Minh City offices of Peregrine Capital Vietnam on May 30, it wasn't a courtesy call. They seized armloads of documents ranging from computer manuals to financial records. And they raided the local branch of the Hong Kong-based investment house, which distributes Johnson & Johnson products, sells Mercedes-Benz cars in Vietnam, of setting up illegal subsidiaries. Charges have been brought, but the raid has sent a chill through the business community.

On the eve of the Communist Party congress opening June 28, the raid is one of the strongest signs yet of Hanoi's move to wrest back central control over the economy, rein in the private sector, and check foreign cultural influences. Ten years after launching the economic reforms known as *doi moi*, party leaders want to show investors they're boss. No new reforms have been instituted for 18 months, and in a key report released prior to the congress, the party vowed not to let the country stray onto the capitalist path. To bolster the forces of central control, it also recommended upping the share of the private sector from 40% of gross domestic product to 60% in the next 25 years.

Analysts say the chill on reform reflects a struggle by party conservatives to regain the upper hand. While *doi moi* has unleashed an unprecedented period of growth, the reforms also have created a class of rich entrepreneurs, whom ideologues see as a threat to their monopoly on power. "If you want growth, you have to allow the private sector to grow," says a diplomat in Hanoi. "But if you get a strong private sector, it will seek political control."

OFFICIAL APATHY. Healthy economic performance is another reason the party has stalled on reform. Annual GDP growth has averaged more than 8% over the past five years, and the triple-digit inflation of 1989 has been tamed, to below 10%. International donors have pledged more than \$4 billion in aid over the next three years, while foreign investors looking for Asia's next tiger have pledged \$22 billion since 1989.

But things aren't as rosy as the figures suggest. Outside investors are turning increasingly downbeat, fearing hardliners in the government and the party will jeopardize

WHAT THE HARDLINERS WANT TO DO:

- Increase role of state sector in the economy
- Impose tougher controls on foreign investors
- Resist foreign cultural and political influences

DATA BUSINESS WEEK

COMMENTARY

By Amy Borrus and Joyce Barnathan

IT'S TIME TO GET CHINA INTO THE WTO

A sense of déjà vu is settling over U.S.-China trade relations. For the third time in four years, the two economic giants have edged back from the brink of a trade war. On June 17, Acting U.S. Trade Representative Charlene Barshefsky reached a last-minute agreement on intellectual-property rights with Beijing trade officials that prompted Washington to withdraw threats of punitive sanctions against Chinese imports. In the U.S., there is relief that the latest accord will close 15 plants in China pirating compact discs. The deal also calls for greater market access and copyright protections for U.S. films and music recordings.

But there is also mounting frustration that America's trade cops are continually waging high-stakes battles for piecemeal gains. The risks inherent in the Administration's Lone Ranger stance were clear in the recent show-down. Angered by U.S. threats of punitive tariffs on \$2 billion worth of Chinese goods, Premier Li Peng hinted he'd steer coveted contracts to Europe. No wonder Europe hung back while the U.S. played bad cop. "Acting unilaterally is no longer as effective as it once was," says David Rothkopf, managing director at Kissinger Associates. "Our chances for greater leverage and fewer crises come from being able to build coalitions."

TARIFF COP. In the short run, whether the issue is intellectual piracy, market access, or abuse of textile quotas, the U.S. must still hold China's feet to the fire with threats of sanctions, or, better yet, subtler punishment. But over the long run Washington officials must recognize that repeated bilateral trade battles will leave America isolated. The solution: It's time for the U.S. to focus more forcefully on getting China into the World Trade Organization (WTO). And with both the U.S. and China showing an eagerness for warmer ties, Washington has a golden opportunity.

WTO membership would oblige China to follow international rules. With Beijing in the club, the U.S. would have a better shot at marshaling global support if China breaks them. While the trade court has little authority to mediate the fuzzy issues of cartel-like business practices that are at the heart of many U.S. trade beefs with Japan, WTO rules do cover



ELEVENTH HOUR
Barshefsky swung a deal—but the U.S. should avoid such oil changes as often as possible

as being allowed to treat foreign companies differently from domestic firms. The U.S. and other nations insist that Beijing must commit to legal and economic reforms before it can become a member. Joining the WTO would also force Chinese companies to lay off perhaps millions of workers, as they gird for an onslaught of foreign competition. And China would have to pay fines or other compensation if it violates WTO rules. "All they see are the costs; we have to think creatively about incen-

tives," says Nicholas R. Lardy, senior fellow at the Brookings Institution.

That doesn't mean U.S. and other WTO member nations must lower the admission standards for Beijing. Its economy is too big to risk letting China be a free-rider in the global trading regime. But there ought to be flexibility in phasing in conditions for China's membership.

MAJOR IRRITANT. Washington should also offer Beijing a sweetener in the form of permanent most-favored-nation (MFN) status. That could spark renewed interest in Beijing in joining the WTO. China's enthusiasm fizzled when it realized that entry wouldn't necessarily end the annual U.S. review of its trade status. Yearly debates over MFN have been a major irritant in the relationship. China's critics in the U.S. Congress use the occasion to beat up on Beijing for everything from forced abortions to arms trafficking. By changing the law requiring an annual review, "there would be a lot more motivation for China to want to get into the WTO," says a Western diplomat in Asia.

Critics of China and the WTO argue that the U.S. benefits most by keeping Beijing outside the global trading regime. If China were a member, they say, WTO rules barring unilateral sanctions might undercut American leverage in trade disputes with Beijing—as they have with Tokyo. That's true, but the upside potential of Chinese membership—once Beijing meets conditions for entry—outweighs the risks.

For now, the U.S. has no choice but to keep the heat on China. Declaring victory in the face of blatant violations would undermine U.S. credibility, not just in China but throughout Asia. But while pressing the Administration had best keep its eyes on the future. Once in the WTO China would be under concerted international pressure to play by established rules.

Borrus in Washington and Barnathan in Hong Kong follow U.S.-China relations for this magazine.



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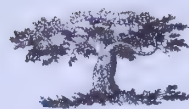
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THE HEADACHES AHEAD IN YELTSIN'S SECOND TERM

President Boris Yeltsin's slim victory in the June 16 first-round election leaves him in surprisingly good shape to beat his Communist rival, Gennady Zyuganov. Although Communists won 32% of the vote, compared with Yeltsin's 35%, they are losing momentum as the President surges ahead. As Yeltsin maneuvers to consolidate his lead, it is already possible to discern outlines of his new administration. Assuming he wins, the election process should refocus Yeltsin and return him to the reform path. The campaign forced him away from his closed-door advisers and put him in closer touch with ordinary people, 57% of whom backed reform candidates. Thus, a second Yeltsin government would likely crack down on corruption and be more committed to market reforms, albeit with a softer start regarding social concerns.

CHAOTIC INFIGHTING. Yet the price of Yeltsin's staying on could be steep. He has dug Russia into a deep financial hole, and he could be sowing the seeds of vicious infighting by quickly giving a top job to maverick former General Alexander Lebed. Hoping to win over the surprising 15% of the voters who went for Lebed, Yeltsin made the gruff nationalist overseer of defense, police, and intelligence agencies. At the same time, he sacked Defense Minister Pavel S. Grachev, who has been tarred by the bungled operations in Chechnya. Already, Lebed, 46, is being talked about as Yeltsin's successor—a serious matter, considering the 65-year-old leader's erratic health. Lebed is a mixed bag for the West. He is against NATO expansion but strongly opposed to the war in Chechnya. But he is likely to focus mainly on domestic affairs. He says his mandate is to lead a war against crime and corruption. There's even speculation that he may use elite shock troops rather

than ordinary cops against criminal gangs. Such G-man tactics will please the public and entrepreneurs fed up with shake-downs by mobsters.

Indeed, Lebed, who made his reputation by blasting Grachev over alleged military corruption and Chechnya, could be an unguided missile. He is already accusing senior generals of plotting against Yeltsin. And Lebed, who has no experience in Kremlin jockeying, could be outmaneuvered by such wily Yeltsin allies as Prime Minister Viktor S. Chernomyrdin and Moscow Mayor Yuri Luzhkov. He could well clash with these insiders if he goes after their business buddies.



LEBED: *He could be an unguided missile*

Along with Lebed, some of the old reformers are likely to regain influence. One comeback candidate is former privatization chief Anatoly B. Chubais, whom Yeltsin cashiered last winter under pressure from the Communists. Despite this callous treatment, Chubais and other free-marketers helped mastermind the Yeltsin campaign, and they seem due for rewards. Whatever aides wind up running state finances will

have their hands full. Given Yeltsin's free-spending campaign, the government has been staying afloat by issuing short-term bonds. A new government may have to raise taxes.

Still, the majority of Russians seem disposed to give Yeltsin time to put his stamp on the emerging country. They think the current system with all its drawbacks is preferable to a closed regime under the Communists. "I voted for Yeltsin because he represents stability. I'm afraid of any abrupt change," says Emilia Y. Koroleva, 55, a doctor from the industrial Moscow suburb of Lyubertsy. That seems to be a good summation of mainstream thinking.

By Peter Galuszka and Patricia Kranz in Moscow

GLOBAL WRAPUP

ITALIA RESCUE

Italy's troubled airline Alitalia finally has a turnaround plan that both management and labor endorse. Dominic Cempella, chief executive of the state-controlled carrier since May, had threatened to shut down operations unless the unions approved draconian cuts to stem huge losses. In June 19, the unions caved in, agreeing to 3,000 job cuts over five years. Remaining staff will work longer hours for lower wages. In exchange, the unions get a 20% equity

stake and three seats on the 15-member board of directors.

Employee ownership is a novel concept for a public-sector Italian company. The idea may help overcome union resistance to restructuring at other state-owned assets, such as the national railroad. The agreement also signals a tougher approach by the government toward labor. Alitalia's parent, state holding company IRI, had held back a capital infusion of \$1.9 billion until the unions had agreed to Cempella's plans.

Cempella can now work on making

Alitalia profitable and preparing for privatization. The planned layoffs—about 17% of the workforce—will help solve the basic problem of bloated labor costs, which are some 30% higher than those of such key competitors as British Airways and Lufthansa. Says Flavio Cereda, an analyst at brokers Alfred Berg in London: "For years, the carrier has been run more like an employment agency than a competitive airline." Once employees are owners, they may view such featherbedding more skeptically.

By Silvia Sansoni in Rome

MOVIES

LIGHTS, CAMERA, LESS ACTION

With costs out of control, Hollywood opts for fewer films

Last fall, workers hired by Warner Bros. Inc. spent weeks transforming the facade of a New York City building to resemble CIA headquarters. The building was to be used in a crucial scene in *Eraser*, the latest Arnold Schwarzenegger action film. But two days after flying in from Los Angeles, the film's crew and stars left without ever shooting a scene. The reason? Last-minute rewrites of the script made the scene unnecessary.

Plagued by this and other instances of poor planning and lax cost-controls, *Eraser* exceeded its \$70 million budget by at least \$40 million when it premiered on June 21. Hit or miss, it is yet another big-budget movie in an increasingly crowded field. This year, Hollywood's major studios will release 171 movies—13% more than last year. Next year, there will likely be fewer major-studio releases but far more big-budget ones: Seven will cost an astonishing \$130 million apiece to produce and market. Notes one major studio chief: "We look at each other and wonder how we could be so stupid. We spend too much, we produce too many films, and then we cry that this is a lousy business."

The fundamentals of the movie business are shifting, and glum studio executives are realizing that their industry—never high-margin—is getting even tougher. While average



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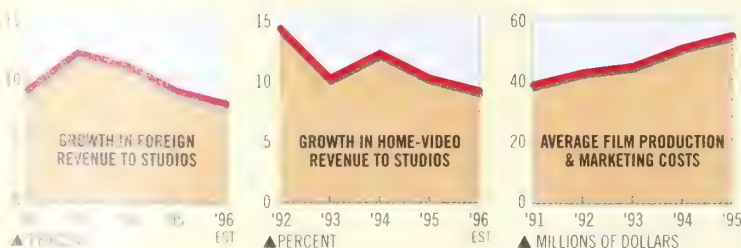
GO FIGURE

"We... wonder how we could be so stupid. We spend too much, we produce too many films, and then we cry that this is a lousy business"

per-picture production and marketing costs climbed 42% between 1991 and 1995, to \$54 million, revenue growth from foreign and home-video sales has slowed (chart). Operating margins have fallen from 11% in 1990 to 7% this year, says John Suhler, president of media investment firm Veronis, Suhler & Associates. Says Thomas Pollock, former chairman of MCA Inc.'s studio operation:

films in the market that if your doesn't catch immediately, theaters will get rid of it and put in something else," says Sony film chief Mark Canton. Suhler, for one, is not convinced the reduction cuts will have any lasting effect: "The fact is that, over the haul, the amounts studios spend to do to their asset base always grow faster than their revenue."

THE NUMBERS IN HOLLYWOOD AREN'T ADDING UP



DATA: MOTION PICTURE ASSN. OF AMERICA, VERONIS, SUHLER & ASSOCIATES

"The smarter people are starting to realize that they can't continue to spend these sums."

SLEDGEHAMMERS. But the industry's still run deep and will be tough to reverse. In a cluttered marketplace, studio chiefs feel pressured to spend ever more on special effects, big stars, and publicity to differentiate one film from the pack. And the free-spending culture in Hollywood is so entrenched that executives are using sledgehammers rather than scalpels to attack the problem. Instead of managing costs of individual projects more adroitly so that films are delivered at a cost studios can still profit from, many studios instead are slashing the number of movies they will release.

On June 10, Walt Disney Co., which has the biggest box-office market share in the industry, said it would halve its annual output to only 20 movies. Paramount Pictures Corp., a unit of Viacom Inc., will release only 15 or 20 films next year, rather than the 25 it had forecast a year ago. Sony Corp.'s Columbia Pictures and Star studios will release 28 films this year, down from 35 released in 1991. "There are so many

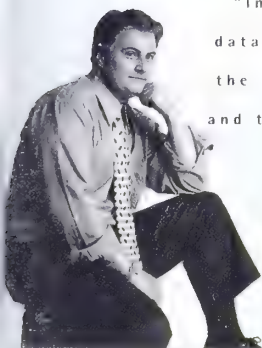
Why is the problem surfacing now, when tales of spending excess go back decades? In the past, much could be masked as new areas, such as foreign markets, home video, and pay-per-view, poured revenue into studio coffers. But that is no longer the case, according to data provided by Veronis, Suhler & Associates. "The movie markets aren't making

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alizing for Hollywood products as fast as the industry had anticipated. The home-video market, which provides 26% of studio revenues, is growing half as fast as five years ago. Box-office revenues have climbed only 10% since 1990, and that is largely thanks to ticket-price increases, not any real gain in the number of people going to the movies. Growth in pay-TV sales has slowed as well. Foreign-sales growth is tapering off, and interactive technologies such as video on demand have not yielded any new revenue streams.

Although many studios are dealing with their industry's woes by cutting the volume of movies, there is little, if any, appetite to trim the budgets of films already given a green light. Star actors and directors have assumed so much power that it is nearly impossible for studio executives to exert much fiscal control once a project has been approved. Take *The Mirror Has Two Faces*, which Barbra Streisand is directing and directing for Canton's Tri-Star studio. After the production was already under way, Streisand abruptly fired not only star Dudley Moore but many of the production and lighting technicians. Production was halted as Streisand hired a new actor, George Segal, and a new crew.

STAR WORSHIP. The brouhaha helped drive the price tag up 26%, from \$35 million to \$44 million. Sony acknowledges that there were problems on the set, although a spokesperson says that "you know what you get with a Barbra Streisand film. Sure, there may be the problems of a perfectionist, but you also get a great film." And on the set of *The Double*, which is being made by former Sony studio chief Peter Guber's production company for Columbia to distribute, star John Travolta quit over creative differences with director Roman Polanski after rehearsals had already begun. Panicked, the producers had to pay Steve Martin \$12 million—far more than his going rate—to take Travolta's place.

These two episodes illustrate what executives treat as Hollywood's most sacred tenet: Audiences want stars. Sure, they can cut production, rein in overhead, and look for partners to share risk. But in the end, studios feel a big film has to have a big star, and they pay ever-skyrocketing fees to get them. Even though he hasn't had a major hit in years, Sylvester Stallone still commands \$20 million a film. If you're green-lighting his next movie—and someone always will—all you can do is cross your fingers and hope the film will somehow defy the economic reality now settling in on the movie business.

By Ronald Grover in Los Angeles

The Corporation

MERGERS

UNION PACIFIC'S UPHILL HAUL

Foes say its bid for Southern Pacific is anticompetitive



Exulting over a major legislative victory last December, Union Pacific Corp. chief Drew Lewis let his guard down. For months, Lewis had been engaged in an all-out lobbying battle to convince Congress to create an independent board to review railroad mergers. Convinced that such a board would be more likely to approve his controversial \$5.4 billion bid for Southern Pacific Rail Corp. than the trustbusters at the Justice Dept., Lewis left little to chance: From making UP's pitch directly to House Speaker Newt Gingrich to attending obscure subcommittee meetings, Lewis personally led UP's legions of lobbyists.

So when the Senate gave its final O. K. to create the Surface Transportation Board four days before Christmas, Lewis decided to celebrate. "I had two drinks on the way home," he recalls. "It was a good day in Washington."

For Lewis, who just a year earlier had taken a month-long leave of absence to attend an alcoholism rehabilitation program, the good day quickly turned sour. Driving his Ford Explorer

south in the not bound lane of eastern Pennsylvania highway after the former U.S. Transportation Secretary was picked over by a state trooper. After failing sobriety tests, Lewis was fined \$300, and his license suspended for three months and was put on probation. He says he has since stopped drinking.

Lewis' ill-fated celebration also appeared to have been premature. In the wake of the Senate victory, opponents say, Union Pacific figured it would easily win approval for the Southern Pacific deal. But some powerful foes have since

CEO LEWIS: A deal would put UP in the No. 1 spot again

up against the merger. As the endgame draws near—the STB's preliminary decision is due on July 3—Lewis is facing a far tougher fight than expected.

CONSOLIDATION. It's a battle he doesn't want to lose. The 64-year-old CEO is retiring this fall after nine years at the helm and a long career mingling business and high-level Republican politics. Determined not to leave the 127-year-old railroad running behind Burlington Northern Santa Fe Corp., Lewis wants to cap his record with the merger, which would again make UP the nation's biggest railroad. "This will be his crowning achievement," says John R. Meyer, Harvard economics professor and longtime UP director.

Bragging rights aren't all that Lewis is after. As the rail industry consolidates, he argues that bigger is better. While UP, headquartered in Omaha, Pa., was long the strongest player

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The Corporation

the West, the combined Burlington and Santa Fe threatens it and, Lewis claims, gives too much market power to one carrier. Lewis says a link with San Francisco-based SP would also keep UP strong if eastern railroads merge in coming years. "Strategically, this is the most significant move the railroad has made in the last 50 years," he says. "I'm not doing this for an ego trip."

Still, a deal would be something of a balm for Lewis: He lost the Santa Fe to Burlington Northern in a bidding contest in late 1994. The merger would also be the culmination of Lewis' efforts to bolster UP's transportation business while cutting costs and shedding units from a

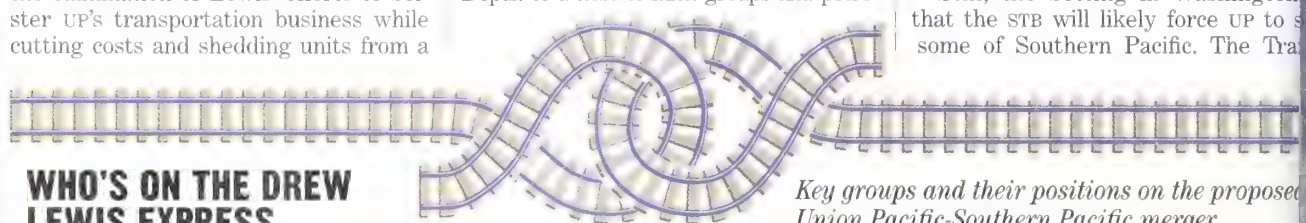
worries rivals and rail users. The biggest fear: Roughly 90% of all rail transport between the U.S. and Mexico would end up in UP's hands. This and other concerns led both the Texas Rail Commission and the U.S. Justice Dept. to oppose the merger. Officials at Justice also worry that UP-SP would have a stranglehold on key lines connecting Texas to Chicago and to the Southeast, and cut competition in the West.

UP says it expected flak from Justice Dept. trustbusters. But other opponents, from the Transportation and Agriculture Depts. to a host of farm groups and petro-

have weighed in with every senator or perhaps 60 representatives. "We've done our homework," he says.

SPIN-OFFS. The legwork has paid off: 21 states support UP, including California. Lewis and Davidson have also built a stable of corporate backers, including SP customers who figure UP's plan to spend \$1.3 billion upgrading the cars will improve poor service. In all, some 1,300 shippers back UP. One-time opponents Monsanto Co. and the influential Chemical Manufacturers Assn. have withdrawn opposition.

Still, the betting in Washington is that the STB will likely force UP to sell some of Southern Pacific. The Tra-



WHO'S ON THE DREW LEWIS EXPRESS

Key groups and their positions on the proposed Union Pacific-Southern Pacific merger

ABOARD

ON THE PLATFORM

CHEMICAL MANUFACTURERS ASSN.	Withdrew opposition when assured rival railroad would have access to tracks
OFFICIALS FROM CALIFORNIA, 20 OTHER STATES	Say deal will promote efficiency
PORTS OF SEATTLE, PORTLAND, TACOMA, OAKLAND, NEW ORLEANS	Expect better service from SP line upgrades
EXXON, COORS BREWING, GENERAL MOTORS, CONAGRA, 3M	Anticipate better shipping service
LABOR UNIONS AT SP AND UP	Most figure merger will protect jobs

JUSTICE, TRANSPORTATION, AND AGRICULTURE DEPTS.	Charge deal is anticompetitive
RAILROAD COMMISSION OF TEXAS, SOCIETY OF THE PLASTICS INDUSTRY, NATIONAL INDUSTRIAL TRANSPORTATION LEAGUE	Fear high shipping costs
KANSAS CITY SOUTHERN INDUSTRIES	Concerned about rival's dominance
CONSOLIDATED RAIL	Wants parts of Southern Pacific for itself

long-abandoned diversification. Last year, for example, Lewis snapped up the 72% of the Chicago & North Western line that UP didn't own, and he plans to spin off the company's 83% stake in energy subsidiary Union Pacific Resources.

SKEPTICAL. The clean-up seems to be putting UP on track. Although earnings, excluding one-time charges and the resources unit, grew just 2.3%, to \$605 million, on revenues of \$7.5 billion last year, analyst Anthony B. Hatch of NatWest Securities Corp. expects 1996 profits to jump 22%, to \$736 million. Adds Kevin A. Melich, portfolio manager of Delaware Investment Advisers, which holds 2.68% of UP's stock: "Lewis' strength has been in putting together a good franchise" through acquisitions and refocusing on railroads. Still, many on Wall Street appear skeptical that UP will achieve its acquisitive aims. Shares have risen just 4%, to about \$69, since the August bid.

It's the very size Lewis seeks that

chemical companies, have also inundated the STB with complaints (table). The heavy opposition makes it increasingly unlikely that Lewis' deal will survive unscathed.

To regain momentum, UP is counting on Lewis' blend of political and business savvy. As Transportation Secretary under Ronald Reagan, whose Presidential campaign he had helped manage, Lewis gained notoriety as the man who broke the air traffic controllers union in the early 1980s. He joined UP as head of its rail line in 1986 but remains a powerful behind-the-scenes political player. A top fund-raiser for Bob Dole, Lewis is using his formidable connections in Washington and nationwide to keep the deal on track.

To concentrate on the battle, Lewis handed over daily operating duties to heir-apparent Richard K. Davidson last fall. Lewis spends much of his time with regulators and politicians. The goal: letters of support or pledges not to oppose the deal. Lewis and his colleagues

portation Dept. argues that UP must vest the Texas lines—a potential deal killer, says UP. The DOT also wants UP strengthen track rights it will give BNSF on routes out of California. Although the STB is independent, observers say can't ignore the federal agencies and members of Congress fighting the deal.

For now, UP's chief argues publicly that he wants all of Southern Pacific. Forced divestitures will "balkanize" the West. Still, few believe Lewis will walk away rather than sell some lines. This doesn't go through, it would be viewed as a personal defeat for Lewis, says one opposing lobbyist. "He's too much invested." Just how much will be willing to give up is unclear. For Lewis, every mile of track lost is a blow: With his business and political skills on the line, anything less than a career-capping victory will hurt.

By Joseph Weber in Philadelphia with Catherine Yang, Christina Valle, and Dean Foust in Washington

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INCORPORATING PRESENTATIONS

Projecting the Corporate Image



Presentations are an integral part of corporate life. Everyone from CEOs and middle-level managers to salespeople and training personnel regularly find themselves standing before an audience trying to communicate.

For some, like those participating in sales or training teams, presentations can be daily occurrences. For CEOs and departmental managers, a presentation may be more of a special occasion. But in either case, capturing the full attention of an audience and conveying information in clear and interesting ways are the keys to successful communication.

When the time comes to deliver that presentation you've worked so diligently to prepare, you want to make sure your audience can see what you're talking about. That means you need to consider which type of display system is required to ensure that presentation images are sharp and clearly visible to the entire audience. These days, there are many from which to choose.

Display system choices include large-screen presentation monitors, portable LCD panels, LCD projectors, and CRT projection units. Each of which provides a unique solution, tailor-made for the size of the audience and the circumstances of your venue.

Bigger Is Better

When your audience numbers only one or two people, it's not out of line to use your desktop computer's monitor as a presentation display device. But when three or four people are present, it becomes cumbersome for everyone to crowd around, or if seated at a table to see clearly from the far end of the room.

In such situations, the solution is a presentation monitor, units that range in screen size from about 25 inches to over 40 inches.

Presentation Monitors

Among the manufacturers of presentation monitors are Aydin, Barco, General Video, JVC, Ikegami, Mitsubishi, NEC, Panasonic, Phillips, Presenta, and Sony. Prices range from around \$2,000 to over \$13,000, depending on the model's size and capabilities.

Presentation monitors are best suited to relatively intimate settings, such as board rooms, conference rooms, and training-center classrooms. For example, these monitors can be the centerpiece of a boardroom media wall.

However, presentation monitors can also be linked together to provide secondary displays in a large hall, and they are also suitable to locations where small groups of people can

easily congregate around the screen, including the public areas at corporate headquarters and even the brightly-lit, open-spaces of trade shows.

Essentially, large-screen presentation monitors are bigger versions of the monitors used with desktop computers, but there are internal differences. The most significant is the size of their pixels, usually referred to as the monitor's "dot pitch," and normally measured in millimeters. Most modern computer monitors have a dot-pitch ranging from .26 to .28 mm, while presentation monitors are usually in the range of .7 to .97 mm.

Dot pitch measures the size of the openings in the monitor's shadow mask, a mesh that sits between the monitor's electron gun and the phosphors embedded in the screen. It's the electrons shot through this mesh that excite the phosphors to produce the image, and generally speaking, the smaller the dot pitch, the sharper and crisper the image.

Most presentation monitors are variable scan displays, so they can synchronize themselves to signals from a variety of sources, and most accept input from Macintosh and PC computers.

The type of presentations you create will determine how much resolution you need.

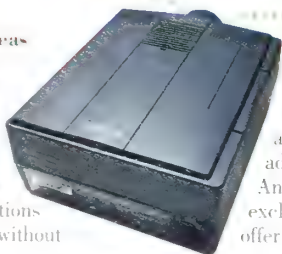
Most models also offer around 600 lines of resolution for NTSC video and 800 by 600 resolution for computer input, but some units only provide 640 by 480 displays and others go up

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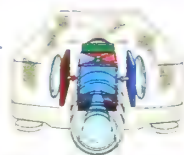
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to 1280 by 1024 resolution. In most cases, the lower or middle-of-the-road-resolution models will do just fine. But if you need to display highly-detailed images crisply, CAD drawings for instance, then it's worth investing in one of the higher-resolution models.

Other things to consider are ease-of-use issues, like the accessibility of video controls, whether the model uses a wireless or tethered remote, and whether it provides built-in speakers. For example, if you're one to walk around while presenting, a tethered remote may be a constraint, whereas someone else might find a wireless unit too easy to misplace.

LCD Panels & Projectors for Portable Brilliance

In recent years, LCD (Liquid Crystal Display) panels and LCD projectors have become popular presentation display systems. Similar in operation to the LCD screens common to portable computers, these devices are connected to the video port of a computer and let you project images on a wall or a movie screen. Combined with a laptop, these devices are excellent for travelling presentations.

LCD panels are designed to be portable, however, projectors can weigh up to 30 pounds, so they fall more in the luggable category. Nonetheless, many LCD projectors come with carrying cases so they can earn their keep on the road.

Panels are designed for use with overhead projectors (OHPs), while LCD projectors are stand-alone units combining

the LCD display, the light source, and the projecting optics. Prices for both types of devices range from just under \$2,000 to over \$10,000.

Manufacturers offering portable LCD panels include: 3M, Apollo, ASK LCD, Boxlight, Chisholm, CTX International, Davis, Dukane, InFocus Systems, IntelliMedia, Megapower Technologies, Minnesota Western, nView, Panasonic, Panel Light Display Systems, Polaroid, Proxima, Sayett Technology, Sharp Electronics, Telex, and VRex.

Manufacturers offering LCD projectors include: 3M, Apollo, ASK LCD, Barco, Boxlight, Davis, Dukane, Eiki Multimedia Products, Epson America, Fujitsu MicroElectronics, Hitachi Multimedia Systems, InFocus Systems, Megapower Technologies, NEC, nView, Panasonic, Phillips, Polaroid, Proxima, Sanyo Industrial Video Division, Sayett Technology, Sharp Electronics, Sony, Telex, UnicView and VRex.

LCD Panels are flat devices, square or rectangular in shape.

Generally, they're about the thickness of a laptop computer and weigh in the neighborhood of seven pounds.

For good quality images, most panel manufacturers recommend that you use OHPs that can produce a minimum of 3,000 lumens, a standard measurement of light intensity. However, to produce clear images in rooms with higher levels of ambient light, you may need an OHP with greater light output. Consult your manual to make certain the light intensity remains within the panel's specified operating parameters.

The screens of LCD panels range in size from about eight inches to

over ten inches, measured diagonally. The smaller panels produce images at 640 by 480 resolution making them compatible with Macs and most PC display controllers. They can project images as large as 10 feet diagonally, suitable for use in normal size conference rooms. The larger 10 inch panels can produce 1024 by 768 resolution and project larger images, making them suitable for spaces as large as a small auditorium. However, they usually cost more than \$10,000 and need brighter (over 4,000 lumens) OHPs to work effectively.

Like the LCD screens of laptops, LCD panels can be passive or active matrix displays. Without delving too deeply into the technical issues, with active displays the LCDs respond to, and recover from, the display signal more quickly, resulting in faster screen refresh rates. In practice this means active matrix panels produce



sharper, clearer, more steady images and better color reproduction. That might not be critical with relatively static presentations, but if you intend to project high-quality photo images, a multimedia presentation, or live video, an active matrix display is absolutely essential.

Projectors use the same size LCD matrix as do panels and are entirely self-contained. Of course, they're bulkier and heavier than panels, usually weighing in at 20 to 25 pounds, but you're spared having to find the correct type of OHP with the proper amount of illumination. And since the light source is built-in, it can be

matched to the characteristics of the LCD display. So projectors usually produce higher quality images, and work better in locations with a high degree of ambient light.

Beyond their ability to display images, LCD panels and particularly projectors usually come with a variety of features to make presentations easier. In addition to computer connections, panels and projectors often provide plugs for other video input sources. Many models can also display multiple signals simultaneously, letting you mix computer output with video images.

Of course, products often differentiate themselves with individual features. If you like to emphasize your points with handwriting or quick sketches, Chisholm's Rainbow-series panels include a digitizing tablet that lets you write over the displayed image. The Sharp QA-1500 LCD panel provides a port for attaching PCMCIA cards, letting you run a presentation stored in the card's memory. The Phillips LC3000 and LC 2100 projectors come with a built-in, cable ready TV tuner. And, the VRex VR-2010 projector and the VR-1000 panel are designed to project 3-D stereoscopic images.

IntelliMedia offers panels with built-in 486-based PCs, to which you can attach a keyboard as well as other PC peripherals.

Working in the opposite direction, both IBM and Revere technologies offer portable computers with LCD screens that detach to become projection panels, for the ultimate in portable presentation systems.



The Sharp QA-1500 LCD Panel

CRT & Light Valve Projectors: Getting the Big Picture

Although LCD panels and projectors have made great technological strides, if you want really large, bright, high resolution images CRT and light



valve projectors are still the best solution. These projectors are decidedly high-end products, intended for permanent installation in locations such as boardrooms and corporate auditoriums. Prices range from just over \$4,000 to tens of thousands, with some models well into 6-digit numbers.

Manufacturers offering CRT and light valve projectors include: AmPro, Barco, Electrohome, Envision, NEC, Hughes/JVC, Mitsubishi, Panasonic, Science Applications International, Sony, Spectrel, and UnicView.

Most CRT projectors use three separate phosphor-coated tubes (red, green, and blue), each with its own video amplifier and lens system. The three images are projected onto the screen where they merge to form the final image. They usually offer automatic convergence features, but since alignment is dependent on the actual distance from projector to screen, getting precise alignment usually involves some fine-tuning of the controls.

Light valve projectors use several different imaging systems, including LCD and CRT technologies. Usually these projectors use a single lamp and lens system and a dichronic filter divides the light into red, green, and blue components. The three beams are modulated according to the image, then are recombined and projected on the screen. These projectors are divided into several categories—video, data, graphics, and super graphics—according to their horizontal scan rate. Video projectors can accept standard NTSC video signals at 15.75kHz. Data

projectors accept signal frequencies from 15 to 37kHz, suitable for text based computer output. Graphics projectors can accept frequencies from 15 to 80kHz, making them suitable for handling more complex images, while super graphics models can handle frequencies up to 135kHz.

Naturally model costs rise accordingly, so your first job is to determine the intended use of the projector. However, if you're looking for portability, you're out of luck. Although one or two models weigh



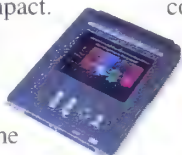
in under 50 pounds, the majority tip the scales at several hundred and some even weigh more than 1,000 pounds. Obviously the majority of these projectors are for permanent installations. ■



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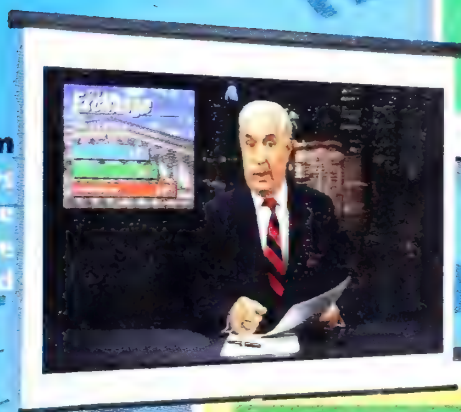
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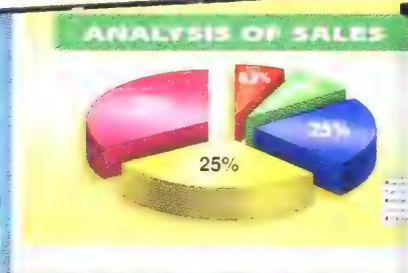
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Presenting With CD-ROM

In a corporate training setting, a CD-ROM based course of study allows employees to proceed at their own pace and to painlessly revisit difficult subject areas without embarrassment—resulting in higher levels of knowledge retention.

Most people think of presentations as being synonymous with standing up in front of an audience, but that's no longer true. These days you can give a presentation without having to be there in person, or even in direct electronic communication with your audience. The medium of CD-ROM has made it possible.

Physically identical to audio CDs, CD-ROMs are intended for use with desktop computers or dedicated players, such as game machines and CD-I (CD-Interactive) systems for the home. CD-ROMs can hold images, sound, text and computer programs, with each disk storing as much as 640 MB of information, sufficient data space for a complete multi-volume encyclopedia. With so much storage

the recipient has the hardware to view your message.

Today many companies routinely produce interactive-multimedia CD-ROMs for everything from sales presentations to corporate training. For example, a sales CD-ROM can make your clients aware of the full range of your products or services, letting them choose from various customizing options, calculate comparative costs, and possibly even give them the simulated experience of using the products. And since CD-ROMs can present information in such engaging form, almost everyone who receives one automatically pops it in the drive to see what's on it. So you're almost guaranteed your message will be seen and heard.

A multimedia application is a program that provides a structure for the presentation's content, control over the combination of media elements, and the interactivity necessary for the user to explore the presentation.

capacity, CD-ROMs are an excellent medium for self-contained, interactive-multimedia presentations.

Once considered a nonessential add-on to desktop computers, today CD-ROM drives are standard equipment on virtually every new computer sold. This proliferation of drives has made CD-ROMs a highly-effective vehicle for distributing presentations, and these days you can be fairly certain

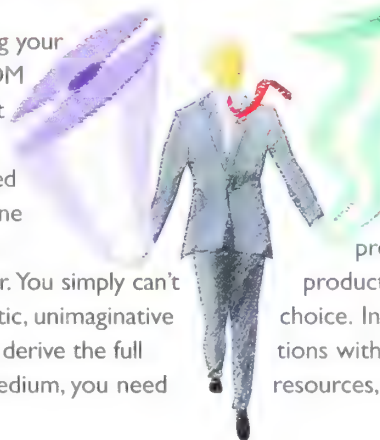
Of course, getting your message on CD-ROM is a bit more difficult than producing a traditional slide-based presentation. For one thing, the audience demands are greater. You simply can't get away with a static, unimaginative production. And to derive the full advantage of the medium, you need

to build an environment where the person viewing the material can interact with it in non-linear fashion, moving back and forth and around the subject matter as necessary.

This means that creating a quality CD-ROM-based presentation requires building a multimedia application with a professional-level authoring system.

Among the products suitable for full-fledged multimedia authoring are: AimTech's IconAuthor for Windows, Allen Communication's Quest, American Training International's TourGuide for Windows, Asymetrix's Multimedia Toolbook, Computer Teaching's TenCore Authoring System, Global Information's TIE Authoring System for Windows, Intersystem Concepts' Everest Authoring System, Macromedia's Authorware Professional (Mac & Windows) and Director (Mac & Windows), and Oracle's Media Objects.

If your corporation has an experienced production department, you might consider building the multimedia application in-house. However for most companies, contracting with a professional multimedia production studio is a better choice. In fact, even organizations with extensive in-house resources, tend to employ outside



experts for multimedia production. This is especially true for training applications, where organizing the content and presenting it effectively require educational as well as production skills.

CD-R drives are now sized to fit on a desktop alongside your computer, and prices have dropped to between \$1,000 and \$4,000.

But it also applies to multimedia production in general. It stands to reason that professionals who specialize in multimedia work are better able to turn out a quality production in less time than most in-house art or communications departments. They not only have more experience, they've usually developed an arsenal of software tools to speed the work along.

Whichever avenue you choose, the final step is to take the multimedia application to a CD-ROM duplicating service to burn (CD-lingo for writing to disk) the distribution copies. If you're producing anything from several dozen to several thousand CDs, production houses are the way to go. However, if you need to produce small runs on a regular basis, or need to burn pre-production disks to test an application's actual CD-ROM drive performance, you might want to look at CD-Recordable drives.

For several years it's been possible to buy systems that let you produce your own CDs. However, until recently these CD-R (CD-Recordable) systems have been both physically too large and prohibitively expensive for consideration by anyone other than professional CD producers.

That has changed. CD-R drives are now sized to fit on a desktop alongside your computer, and prices have dropped to between \$1,000 and \$4,000. The cost of media has also dropped to about \$10 per disk, making these systems a cost-effective proposition.

Although the CD-R drive burns the disk, it's the premastering

(recording) software that controls the process. CD recording software is usually bundled with the drive, especially if both come from the same vendor, but programs are also

available from various third-party developers. Your choice will depend on your needs and the capabilities of individual programs.

Virtually all recording programs now support multi-session writing, which lets you add data to a disk over several recording sessions.

However, understand that writing

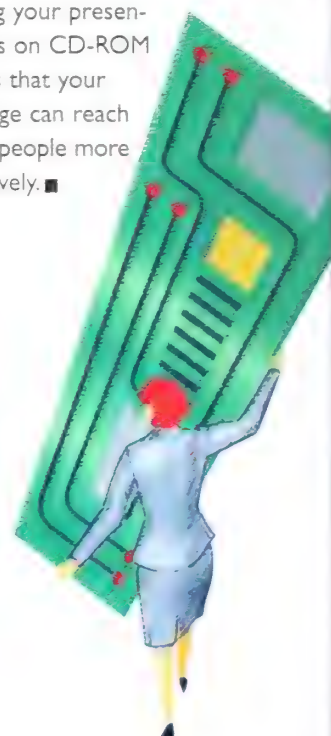
Among the manufacturers offering CD-R drives are: Hewlett-Packard, JVC Information Products, Kodak, Phillips, Pinnacle Micro, Plasmon Data, Ricoh, Sony, and Yamaha. In addition to these manufacturers, there are many resellers that market drives under their own brands.

CD-R drives can be used for general system backup and permanent image and data storage, as well as multimedia production. But if multimedia is your goal, make certain the unit you buy is capable of burning all the formats you need. CD-ROM formats include ISO 9660 (DOS and Windows disks), HFS (Mac), and CD-A (audio). Mixed mode lets you combine audio and data on one disk and Hybrid capability lets you produce disks for use with both Mac and Windows computers. Other formats include CD-I (for the Phillips home entertainment system), CD-ROM/XA (extended architecture—combines CD data with compressed video or audio), and Photo CD (Kodak's image storage system).

CD-ROMs is still a fairly challenging process. Of paramount importance is assuring that the CD-R drive gets an uninterrupted stream of data as the CD is being burned. Premastering software builds an image of the CD on your hard drive and then transfers the data to the CD-R drive. So you need a large-capacity, fast hard disk to ensure that the CD-R drive's buffer is always filled. If the buffer runs out of data, the CD is ruined.

So, given the fragility of the operation, dedicating a computer to the task is a good idea. And if you want to substantially reduce headaches, especially at the outset, choose a Macintosh for the job. It's the best choice for ease of use and compatibility with CD-R systems.

Creating CD-ROM-based presentations is still a daunting process that requires professional-level software and hardware tools to arrive at a quality production. But in the end, getting your presentations on CD-ROM means that your message can reach more people more effectively. ■



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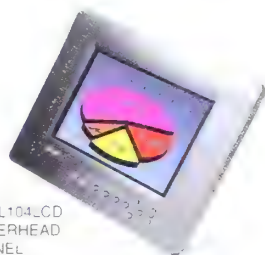
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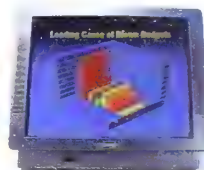
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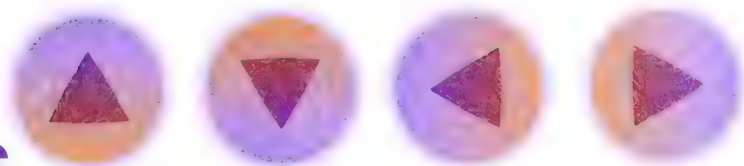
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Content Providers



In the last few years, the style and content of corporate presentations has changed dramatically. The reason is the advent of multimedia—the computerized integration of audio-visual communication technologies. Until recently, multimedia was largely left in the hands of computer-graphics professionals. Today however, creating multimedia presentations is not only possible for most corporate graphics and communications departments, it's even well within the reach of individual business managers.

This is because of more approachable software, not only for the Macintosh, still the leading multimedia platform, but for systems based on Microsoft Windows as well. Traditional, slide-based, presentation programs have also acquired basic multimedia capabilities.

New programs that simplify authoring have also appeared, and even professional-level authoring systems that can generate complex, interactive-multimedia productions have become less daunting.

Nonetheless, the learning curve of high-end multimedia authoring systems remains intimidating. So if you want to get started with multimedia but don't want (or need) to tackle a full-blown authoring system, look at the new crop of general-purpose presentations programs. Easy to use and affordable, presentation programs are often the perfect vehicles for small-scale multimedia projects. And with more manageable learning curves, they make excellent introductory tools for novice multimedia producers.

These programs are aimed at the presentation market but were designed from the start to coordinate

Generally speaking, these programs fall into two categories. The first, consists of the traditional presentation packages, such as Adobe Persuasion (Mac & Windows), Claris Impact (Mac, Windows), Corel's Presents (Windows), Lotus Development's Freelance Graphics for Windows, Micrografx's Charisma (Windows), Microsoft's PowerPoint (Mac & Windows), Novell's Presentations (Windows), and Software Publishing's Harvard Graphics for Windows. In other words, programs that were originally designed to facilitate the production and organization of slides and overheads.

Then there are the second-generation presentation packages, such as Alpha Software's Bravo (Windows), Ask Me Multimedia's Super Show & Tell (Windows), Asymetrix's Compel (Windows), Gold Disk's Astound (Mac & Windows), Multimedia Design's mPower (Mac), Q/Media's Q/Media (Windows), and SoftCraft's Presenter (Windows).

multiple media and display computer-driven productions.

So what should you look for when selecting an entry-level multimedia presentation package? Most presentation programs can produce transition effects (wipes, dissolves, etc.) and moving-typeface-style animations that let you sequentially march topics onto the screen. However, most traditional-style packages now also allow you to incorporate movies in your slides. This has been made possible by the advent of Apple Computer's QuickTime (for the Mac and Windows) and Microsoft's Video for Windows, software that allows your computers to display digital video sequences.

In addition, traditional-style programs have even begun to incorporate hypertext-like features that can impart interactivity to the presentation. For example, with Persuasion 3.0 you can use on-screen buttons to transport the audience to out-of-sequence slides, or even other presentations. So, you're no longer confined to a pre-planned agenda. Depending on the expressed needs of your audience, you can alter the content of a presentation on the fly.

The packages in the second category can more legitimately be





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PROJECTIONS

DIGITAL LIGHT PROCESSING

In the coming months, the first products incorporating a new projection technology should begin arriving on the market. Developed by Texas Instruments this technology is called Digital Light Processing, and in the coming years it may dramatically improve the quality of presentation images.

Texas Instruments has already licensed the technology to a number of projector manufacturers, including nView, InFocus, Proxima, Electrohome, and Sony. The nView Diamond D-400 projector, a 23 lb. transportable model expected in the summer of '96, should be among first out the door.

At the risk of oversimplification, Digital Light Processing (DLP) is based on TI's Digital Micromirror Device (DMD), essentially a RAM chip painted with microscopic

aluminum mirrors that can be individually switched on or off to reflect light.

The DMD chip itself measures about 1 by 1.5 centimeters. The individual mirrors, each corresponding to one pixel, measure 16 by 16 microns, with a distance of only 1 micron separating one mirror from another. The 640 by 480 working resolution of the D-400 is produced by 307,200 individual mirrors in a .625 inch wide area. The light is generated by a high-intensity source, such as a metal halide bulb, located in close proximity to the mirrors.

The first DLP-based projectors will be priced competitively with middle-of-the road LCD projectors. The nView D-400 models are expected to cost \$9,495 and \$9,995 with video capabilities.

with high-end authoring packages. As such, these programs allow you to incorporate basic on-screen interactivity and create reasonably complex productions, all without getting you involved in the intricacies of programming.

However, if you're just looking to liven-up static slides, enhance computer-driven presentations with video clips or animation sequences, or create relatively simple multimedia productions, presentation programs may be able to satisfy all your current requirements.

However, you shouldn't confuse these programs with full-fledged authoring tools. They have neither the power nor the flexibility of true authoring programs, such as Macromedia's Authorware Professional or Director, AimTech's IconAuthor for Windows, and others. If you're planning ambitious projects, such as interactive training modules or stand-alone kiosks, then high-end authoring tools are the way to go.

If that's the case, consider seeking professional help from one of the many independent producers who specialize in creating multimedia marketing materials and interactive-multimedia training courses for corporations. At first, that might seem like an expensive proposition, but when you factor in the learning curve for authoring programs as well as the time required to develop a multimedia application, the cost is reasonable. That way, you get a professional job without having to become a multimedia pro yourself. ■

This supplement was prepared by Carlos Domingo Martinez for Knowledge Industry Publications, Inc., publisher of *Multimedia Producer* and *AV Video* magazines.

Editorial Offices: 701 Westchester Ave., White Plains, NY 10604, (914) 328-9157.

For subscription information contact Mykl Neufeld, (914) 328-9157, fax: (914) 328-2024, E-mail: 72123.353@compuser.com

Content Providers *continued*

called entry-level multimedia tools. With these programs, multimedia capabilities aren't add-ons. Rather, these products have been conceived from the outset to integrate text, graphics, audio, animation, and video elements into well-coordinated presentations.

Multimedia presentation packages usually provide a more extensive production environment than traditional presentation programs. For example, they may include more competent drawing tools for graphics creation. Also, they usually provide more advance animation features,

such as the ability to produce intervening images from keyframes and to define the motion of graphic objects along paths. And, you'll find that they're equipped with better controls for timing and sequencing media elements.

In addition, most multimedia presentation programs come with pre-scripted buttons that can be set to trigger internal events, such as starting a video sequence, or used to launch other linked presentations. And depending on the program, they can even be used to access hardware devices, such as video decks and CD-ROMs, capabilities usually associated

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TELECOM'S PIT BULL

Now Dick Notebaert is guarding Ameritech's turf

The best way to reach Dick Notebaert these days is to zap him E-mail. After his daily 5 a.m. jog along Lake Michigan, the 48-year-old chairman and chief executive of Ameritech Corp. spends time answering employees' electronic queries. Yeah, he's hooked to all things high tech, but he thinks E-mail helps flatten the hierarchy at the longtime monopoly. Sometimes too much. Not long ago, critics chided him about the overgrown grass at headquarters.

One recent morning, though, Notebaert's E-mail concerned the looming battle with the industry's 800-pound gorilla, AT&T. As telecom companies fight for the right to compete in new areas, the squabbling between Ameritech and AT&T has been especially strident. AT&T recently made its first major foray into local service in Ameritech's territory, promising its customers three months of free "local-toll" calls. Ameritech hit back with a deriding the offer as a "gimmick."

TURN FIRE. Then, AT&T CEO Robert E. Allen told securities analysts AT&T should be able to take at least one-third of all phone business in several years, while regional operating companies (RBOCs) could be kept out of long distance until 2000 by the requirement to demonstrate viable local competition. Notebaert told an electronic correspondent: "Allen has been wrong on just about every prediction he has made for several years."

Ferocious, determined, sometimes testy, Notebaert is telecom's pit bull. He and Ameritech are in the middle of one of the biggest upheavals in U.S. business today. The Telecommunications Act of

1996 will open the \$90 billion local phone market to competition and let the Baby Bells into the \$75 billion long-distance business. Analysts say 40% of each market could change hands over five years.

Notebaert, a vocal supporter of competition, must open local service to rivals—but he hasn't let any major players into his yard yet.

Other Baby Bells are teaming up—SBC Communications with Pacific Telesis, Nynex with

Bell Atlantic. Such a horizontal merger "doesn't make sense" for Ameritech, says Notebaert, who notes that joint ventures with the likes of Walt Disney Co. and IBM Corp. have offered merger-like benefits. An acquisition that might tempt him is a company that provides different skills. A cable or software company, perhaps? "Let's just say that if we do something, it'll probably be something nontraditional," he says.

With or without a deal, Notebaert says, deregulation opens the way to great opportunities. Topping the list is long distance, which he expects clearance to enter by the first quarter of 1997. Other opportunities include cellular service, overseas operations, and such nontraditional businesses as security

monitoring and electronic commerce.

Notebaert has set a high hurdle. Despite average revenue growth of 4.5% over the past five years, he has set a goal of double-digit profit and revenue growth off the base of \$13.4 billion in sales and \$2 billion in net income last year. So far, so good: Revenues rose 13% and profits 14% in the first quarter. Shareholders like the CEO's chances. Betsy LaManna, vice-president at stockholder Northern Trust Corp., calls Ameritech "definitely the best of the RBOCs" because of management.

Notebaert seems an unlikely leader for telecom's new age. Since he started out washing trucks at Wisconsin Bell while attending the University of Wisconsin, all his experience has been at monopolies: Ameritech, its operating companies, and, briefly, AT&T. But his willingness to break

with the monopolistic past sealed his success. In 1992, then Chairman William L. Weiss asked some 30 senior executives to describe the future Ameritech. While most

NURTURING A BABY BELL

FINANCIAL First-quarter 1996 revenues rose 13%, profits 14%. Stock soared 52% in 1995.

LONG DISTANCE Plans to enter long-distance business in own territory in first quarter of 1997.

COMPETITION Has struck deals with some local service rivals, but not major players—especially AT&T.

MANAGEMENT Replaced 23% of all managers, 60% of top managers in the past three years.

NEW VENTURES

Has country's No. 2 security-monitoring company, fledgling cable-TV operations, an outsourcing joint venture with IBM, and a growing electronic-commerce business.

SOLO ACT
Notebaert sees no point in hooking up with another phone company



played down competition, Notebaert, then president of Indiana Bell Telephone Co., embraced it. He became a key adviser to Weiss, was named CEO in January, 1994, and succeeded him as chairman a few months later.

Since then, he has finished the sweeping housecleaning begun by Weiss. In three years, 60% of top managers have been replaced. Many new hires come from marketing backgrounds at the likes of Procter & Gamble Co.; Notebaert has a consumer focus despite his career at a monopoly. He has moved Ameritech into consumer surveys, for example, which have prompted changes in Caller ID and voice-mail services.

DOGFIGHT. Away from work, Notebaert—whom an acquaintance calls “almost hyperactive”—pursues rigorous solo sports, such as windsurfing, scuba diving, and skiing. Michael Browning, a friend from Indiana Bell days, says he’s “relentless.” Three months after taking up golf, he entered a tournament. Says Browning: “It’s learn something quickly, and learn it well.”

At Ameritech, he’s putting the same kind of pressure on his top executives by steeply raising performance benchmarks. For example, the small-business services unit, which has been growing twice as fast as the historical rate for business telecom services, is now expected to grow at three times that rate. Still, Ameritech is in for a dogfight. It will probably lose substantial local business in the years ahead, and what remains will be less profitable. If it loses one-third, as AT&T’s Allen predicts, it will have to replace \$1.8 billion in revenues.

To do that, it must get into long distance quickly. Notebaert thinks it should be allowed. Ameritech, he notes, has signed discount agreements with several companies that will resell its services and has agreed to sell parts of its systems to MFS Communications Co. Would-be competitors scoff. Most of Ameritech’s residential consumers have no alternative to local service, they say, because Ameritech has given small rivals access to its system but has frozen out AT&T, MCI, and Sprint. Even MFS will target only businesses.

Notebaert bristles at the idea he isn’t negotiating in good faith. Ameritech’s rivals have their own agenda, he says. They don’t want a competitor with a foot in the door of every customer in its region. No one knows how much Ameritech and other RBOCs will have to bleed before they’re let into long distance. But regulators will surely want to see the entry of at least one major rival before Notebaert gets his wish. Once that happens, his E-mail will deal with far more urgent issues than who’s neglecting the lawn.

By Peter Elstrom in Chicago

Legal Affairs

CYBERSPACE

JUSTICE IS BLIND, BUT NET-SAVVY

How a court was persuaded to overturn the indecency law



The two federal judges arrived early at the Philadelphia U.S. District courthouse on the morning of Mar. 21. But instead of taking their usual seats on the bench, Dolores K. Sloviter and Stewart R. Dalzell started checking the electrical wiring. It was no ordinary day. The first-ever trial of free speech on the Internet was about to begin—complete with a live demonstration of the new medium in the freshly wired chambers. After the third judge, Ronald L. Buckwalter, appeared, the court historian snapped some photos for posterity. “Everyone in the room felt we were involved in making history,” says Chris Hansen, senior counsel for the American Civil Liberties Union.

Three months later, on June 11, the same three-judge panel unanimously struck down as unconstitutional the Communications Decency Act (CDA), which criminalized the distribution of indecent and patently offensive material online. In a sweeping decision, the court said the law, enacted on Feb. 8, violated both First Amendment free-speech protections and Fifth Amendment due-process rights. Wrote Dalzell in one of three separate opinions: “The Internet has achieved...the most participatory marketplace of mass speech that this country—and indeed the

CYBER-JURISTS Dalzell, Sloviter, and Buckwalter. Net newbies at the start of the trial, became fluent in online jargon

world—has seen.... Any content-based regulation of the Internet, no matter how benign its purpose, could be the global village roast the pig.” For the e-culture Internet community, the triumph was a hard-won. When the CDA was signed, users had sunk

a deep funk over what they saw as a shocking government intrusion into their once freewheeling terrain. They cursed their failure to educate Congress about their medium. But for the defeat sprang a winning strategy. “We felt if we could just give the court a feeling of how the Internet functions, they could see that the restrictions would cripple the free flow of information,” says Daniel J. Weimer, deputy director at the Center for Democracy & Technology (CDT). Now, after the CDT and other plaintiffs spent \$750,000 for litigator Bruce J. Ennis and his team, they are preparing for a possible appeal before the U.S. Supreme Court by the

Dept., which had defended the law. The same day the law was signed by President Clinton, ACLU filed its challenge. Its 20 plaintiffs, including Critical AIDS Project, an online site on AIDS prevention and treatment, would show a kind of speech that might be silenced. The group deliberately filed its suit in Philadelphia, where Court of Appeals Chief Judge Sloviter—a Carter appointee—had penned a key decision in 1990 that struck down a dial-a-porn regulation for violating the First Amendment.

UNCENSORING THE INTERNET

FEB. 8, 1996 President Clinton signs the Communications Decency Act, criminalizing the distribution of "indecent or patently offensive material" online. Netizens mourn their loss of free speech rights by turning their Web pages black. The ACLU immediately files a challenge to the new law in a Philadelphia federal district court on behalf of 20 plaintiffs. Another group of plaintiffs files two weeks later.

MAR. 21 On the first day of the six-day trial, the three-judge panel in Philadelphia experiences a live Internet demonstration. A small technical glitch prevents an online tour of the Louvre, necessitating a detour to London museums instead.

JUNE 11 The three-judge panel issues a historic decision to strike down the CDA as unconstitutional because it violates both First Amendment free speech and Fifth Amendment due process rights. The court disseminates the decision via floppy disk.

nt. A coalition, led by the CDR, American Online, and the American Library Association, filed its lawsuit on Feb. 26. The court later combined the two lawsuits. Homework by both teams paid off. At the beginning, none of the three Philadelphia judges was well-versed in the Internet. Sloviter uses a laptop in court to take notes, Dalzell uses a Macintosh Powerbook at home, and Buckwalter only started surfing the Net on his own during the case. On the first day of trial, they were still mulling over terms such as "HTML," a computer language, and "gopher," a search function on the Net. But by the end, they were fluent in cyberspeak, asking whether putting a tag on a URL (labeling a Web site address "for adults only") could help keep kids away from smut. And the normally staid judges seemed charmed with the technology. "The highlights of the case were exciting," admits Judge Buckwalter.

At trial, Netizen witness Ann Duvall, president of SurfWatch Software Inc., which makes software that blocks un-

wanted sites, gave the judges a tour of the Internet, but a technical glitch prevented a walk through Paris' Louvre, necessitating a change of itinerary to London museums instead.

The next day, Robert Croneberger of Pittsburgh's Carnegie Library testified that libraries can't possibly label all potentially indecent entries in their online card catalogs. So, he argued, the CDA could end up banning everything from biology texts (they mention reproductive organs) to Shakespeare (for bawdy language).

"OVERWHELMED." Meanwhile, Justice Dept. witnesses showed how easy it is for children to stumble upon indecent material online, using a search of key words "little women," for the popular novel. Eventually, these led through hypertext links to pictures of naked women. The government stopped short of showing indecent sites, however, and gave the judges a binder of such downloaded materials instead.

In the end, the judges concluded that there was no technologically feasible way now to screen for vaguely defined indecency without violating adults' First Amendment rights. In order to comply with the law, too much legitimate speech, such as online talk of AIDS and library collections, would be curtailed.

Supporters of the indecency statute are outraged. "The judges were overwhelmed by the technology," says Bruce A. Taylor, president of the National Law Center for Children & Families, which champions the prosecution of obscenity. Taylor thinks the Supreme Court will overturn the Philadelphia decision and that courts should define online indecency rather than ban all attempts to regulate online speech.

The Justice Dept. must decide whether to appeal by July 2. Constitutional experts say this High Court may view the Netizens' case favorably. In its past decisions, "the First Amendment has always prevailed," says Washington lawyer John G. Roberts. But like the Philadelphia judges, the justices are unschooled in the cyberphenomenon. If Net advocates hope to get an ultimate win, they may want to help Justice Rehnquist & Co. start booting up.

By Catherine Yang in Washington

THE CARD



Mary and James. Let's just say, don't always see eye to eye. One thing they do agree on, however, is the American Express® Card. That's because the Card is welcomed at all kinds of places, for everything from paper shredders to stuffed animals. (A donkey or an elephant, perchance?)

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THE NEW HUCK

Parents and teachers across the country notice a surge in teenagers sporting electronic beepers this summer. Foot soldiers in a drug cartel? Not quite. Just participants in a PepsiCo Inc. sales promotion. The cut-rate pagers beep weekly messages from sports figures and pop stars flogging soda and other teen-targeted brand-name goods.

TV viewers, used to channel-surfing past the commercials, encounter a strange phenomenon on CBS. On a winter evening, every show during a two-hour period features screen-legend-cum-perfume-vendor Elizabeth Taylor. She wanders in and out of everything from *The Nanny* to *High Society*, searching for a missing string of black pearls—and shamelessly flogging her about-to-be-launched perfume of the same name. No actual commercial airs. In each case, Taylor is part of the story line.

Smokers around the country looking for an alternative to Big Tobacco are confronted with an array of brands with funky names from Moonlight Tobacco Co. Hidden in the fine print on the sides of the distinctive packaging is the name of the real corporate parent, RJR Nabisco Inc.

What happened to the days when logos from America's biggest makers meant quality and integrity and were displayed with pride? When an ad was something that ran in 30-second slots on TV or on a page in a magazine? When commercials actually talked about the products they were trying to sell? Meet the New Hucksters: Part P.T. Barnum-style impresario, part MBA-toting tactician, they reflect the zeitgeist of a generation skeptical of any sales pitch and insatiable in its hunger for nonstop entertainment. In this postmodern advertising, sales messages, once clearly labeled, have now been woven subtly into the culture. Stealth pitches are embedded in movies, TV shows, or made into their own tiny entertainments, complete with fictional histories.

Cover Story

These New Age advertisers are redefining the notion of what an ad is and where it runs. Ads and even products are packaged to hide the big-bucks marketing machines that created them and to obliterate the line between advertising and entertainment and—in some cases—advertising and real life. How? Some marketers aim for an ad that looks as much like an expression of the popular will, and as little like a paid sales message, as possible.

Rejecting the familiar “and now for a word from our sponsor” segue, these advertisers salt the content of a TV show, a movie, or even a video game with product mentions—or better yet, have their brands become part of the story. On the Internet, an online soap opera called *The Spot* builds its plot around the latest advertisers. Other marketers create music-and-celebrity-laced commercials that mimic popular entertainment. That's what Diet Coke did when it got the cast of



Popular culture reflects the pervasive commercialism. TV serials, once oddly devoid of recognizable brands on the set, are now chock-full. The characters on *Seinfeld* shop at Price Club and chew Junior Mints. Over on prime-time sitcom *Ellen*, they watch marketer *extraordinaire* Martha Stewart, in a guest-starring role, sign copies of her real-life cookbook. One of the most talked-about novels of the past season, *Infinite Jest: A Novel* by David Foster Wallace, envisions a time when years are named for their sponsors; most of the story is set in the Year of the Depend Adult Undergarment.

Why are marketers going to such trouble to hide their sales pitches? It's because the buying public has been virtually buried alive in ads. Consumers are bombarded with hundreds of ads and thousands of billboards, packages, and other logo sightings every day. Old ad venues are packed to the point of impenetrability as more and more sales messages are jammed in. Supermarkets carry 30,000 different packages, each of which acts as a minibillboard, up from 17,500 a decade ago, according to the Food Marketing Institute. Networks air 6,000 commercials a week, up 50% since 1983, according to Pretesting Co., a market research company. Prime-time TV carries more than 10 minutes of paid advertising every hour, roughly a minute more than at the start of the decade. Add in the promos, and almost

Some people are so closely associated with their products that they become walking, talking brand names. Whether they're signing a book, guest-starring on a TV show, or grinning in a paparazzo's picture, they're merchandising themselves. Meet Brand Martha and Brand Liz.

To circumvent that clutter, marketers are stamping their messages on everything that stands still. From popcorn bags in movie theaters to airsickness bags on planes to toilet stalls, shopping carts, and gas pumps, few places are innocent of advertising. With total U.S. ad spending up almost 8%, to \$162 billion last year, according to McCann-Erickson USA Inc., the new ad permutations aren't replacing the traditional television, magazine, and billboard messages. Rather, advertisers are adding

new weapons to their arsenals because the traditional venues are packed full.

Even fresh fruit isn't immune. Quaker Oats' Snapple Beverage Div. slapped ad stickers on kiwis and mangoes this spring. It also bought ad space in bowling alleys on the arms that sweep away toppled pins. Lin-gerie maker Bamboo Inc. stenciled messages on Manhattan sidewalks two years ago that said: "From here, it looks like you could use some new underwear." Regina Kelley, director of strategic planning at Saatchi & Saatchi Advertising New York, warns that "any space you can take in visually, anything you hear, in the future will be branded, I believe. It's not going to be the Washington Monument. It's going to be the Washington Post Monument." That may not be such a stretch when cities across the continent have mothballed the venerable names that once graced their sports arenas in favor of the brand names of the highest-bidding advertiser, replacing Brendan Byrne Arena and Boston Garden with Continental Airlines Arena and Fleet Center.

Consumers may loathe the nonstop sellathon, but advertisers are only giving us what we want, or at least what we'll tolerate. The least-zapped commercials on TV are the fast-paced, lavishly produced soft drink spots that lean heavily on entertainment and little on product attributes. But the true postmodern advertising goes even further: It tries to morph into the very entertainment it sponsors. To that end, advertisers have taken up the role of filmmaker, gamemaker, and even novelist in a bid to create messages so entertaining, so compelling—and maybe so disguised—that rapt audiences will swallow them whole, oblivious to the sales component.

Guess? Inc. and Benetton Group both publish imitations of cutting-edge 'zines, with their jarring graphics and jumbled typefaces. Benetton's *Colors*, with a cover price of \$4.50, springs from the same aesthetic—and ad budget—as the retailer's controversial high-shock ads. *Guess Journal*, which has a table of contents, masthead, and bylines, just like a real magazine, features the Guess? brand in most stories. There's either no advertising or nothing but, depending on your point of view.

BEEPER ADS. Knowing that consumers, especially young consumers, have learned to tune out conventional ads, marketers try to infiltrate their favorite entertainment. In Britain, Unilever's Van den Bergh Foods Ltd. is putting the finishing touches on a video game that will star its snack sausage, Peperami. (If you have to know, Peperami does battle with evil snack-food foes Carlos the Carrot and the Terminator.) "This isn't a one-off cheap promotion," says Peperami Marketing Manager Paul Tidmarsh. "We are trying to produce a top-selling game. It is a new way of reaching our target audience." Van den Bergh is not the first. In 1994, M&M/Mars bought a prominent role for its Snickers bar in Nintendo Co.'s *Biker Mice from Mars* video game.

Camouflaging a sales message in a teen's

A NEW GILDED AGE

The History Channel was all set to run a series of company profiles that would have been vetted—and to an extent, produced—by the sponsoring companies. But the concept created such a brouhaha that it ended up on the ash heap.

natural environment was what Pepsi was trying to do, too, when it came up with its beeper promotion. For \$35 and a bunch of Mountain Dew box tops, kids can get a Motorola Inc. pager and six months of free service. The catch? Once a week for six months, they get beeped with an ad. By dialing the toll-free number, they'll hear messages from the likes of Lou Piniella and Ken Griffey Jr. of the Seattle Mariners alerting them to promotional offers and prizes from companies including MTV, Sony Music, and Specialized Mountain Bikes. The promotion has drawn criticism. For

adults, the combination of teens and beepers has only one association: drug dealing, which is why beepers are banned in some schools. Pepsi says the program advocates responsible beeper use. But the controversy isn't all bad for the soft-drink maker. Criticism from grownups may add to the brand's cachet with the young.

Even real life has been co-opted. To help re-promote Hennessy cognac two years ago, ad agency Kirshenbaum Bond & Partners hired models and actors to sit in trendy clubs and order martinis made with Hennessy. Co-chairman Jonathan Bond, who

JUST LITTLE OLD US

Having a giant marketer behind a product used to be an advantage—but not when consumers are searching for something less mass-produced. Companies from Miller to GM to RJR/Nabisco have tried hiding the corporate logo behind a made-up company with a more homespun image.



pany also dreamed up the Snapple Beverage ads, says "word of mouth" technique was not deceptive, even though the buyers didn't identify their employer. "We were trying to give people a chance to evaluate it," he says. People are so cynical that you have to be more inventive just to get considered."

Meanwhile, commercials in conventional formats, such as the 30-second slots in prime time, work hard to blur the distinction between ad and program. MCI Communications Corp. got such a strong response to its Gramercy Press campaign that it extended it to additional media. The soap opera-like TV commercials centered on a fictional publishing house at which all problems were solved and plots furthered with the help of technology. First, a Gramercy Web site appeared. Then came a real novel purportedly written by the campaign's fictional celebrity author Marcus Belfrey and published by the fictional Gramercy Press. The real author, Barbara Cartland, and publisher, Random House Inc., were revealed only inside the dust jacket. MCI even commissioned a two-hour pilot script for a TV series based on the story, but found no takers.

PRIZE ENDING. The Gramercy Press commercials, though full of intrigue, did at least talk about MCI products. Other advertisers have expanded the format and toned down the effort to produce far more subtle commercials. Guess? jeans' latest spot, which aired alongside

views in movie theaters this spring, was a 90-second black-and-white drama starring Juliette Lewis, Harry

Lin Stanton, and the Lords, and Peter Horner.

It had virtually no connection to the sponsor's casual clothing, and even when the angular Guess? logo flashed at the end did audiences find out why had been

running a commercial. A lot of companies go for a degree of entertainment,"

says Guess? President Paul Marciano. "We try to be more entertaining, with a twist of intrigue, mystery."

Whether audiences find it intriguing or manipulative, Marciano is committed to the minifilm format and hopes to extend his next effort to four or five minutes.

But marketers who too aggressively blur the line between advertising and entertainment risk a backlash. Last month, A&E Television Networks' History Channel was forced to scrap plans for a series of one-hour specials that would profile companies.

The highly regarded channel drew heavy criticism for its refusal to allow subject companies to sponsor the series, help prepare the segments, cover some of the production costs, and exercise veto power over the final cut.

A similar uproar over at NBC hasn't quashed plans for *Scan*, a series that will examine the impact of technology on different cultures. IBM, *Scan*'s worldwide sponsor, will own the shows once they air and will sit on an advisory panel, though CNBC says it will retain editorial control. Making things even murkier: Two of the early segments show how priests at the Vatican use computers to digitize ancient religious texts and how commuters in traffic-clogged Bangkok use technology to work as they travel—both subjects of IBM ads in the computer giant's "Solutions for a Small Planet" ad campaign.

Other marketers spin fictions not to disguise their ads but to hide their corporate provenance. The idea is to fake an aura of colorful entrepreneurship as a way to connect with younger consumers who yearn for products that are handmade, quirky, and authentic. The seeds of the genre were planted in the 1980s when

E&J Gallo Winery set up a dummy corporation to avoid using its own name in the ads or on the labels of its new Bartles & Jaymes wine coolers. A campaign revolving around a couple of faux-bumpkin entrepreneurs named Frank and Ed inspired a generation of imitators. "A lot of people seemed to believe they were real, and we never intended that," says Hal P. Riney, head of San Francisco ad agency Hal Riney & Partners Inc., which created the ads.

INSTANT TRADITION. There is a direct line from Gallo's Bartles & Jaymes to Miller Brewing Co.'s Red Dog, which masquerades as a microbrew under the name Plank Road Brewery, and to RJR's Moonlight Tobacco Co. Moonlight markets cigarette brands with such quirky names as Politix, City, and North Star in selected markets. The cigarettes come in packages with eye-catching graphics and only the barest mention of their Big Tobacco parent. "People are looking for more per-

Cover Story

MOCK 'ZINES

If sponsoring the content is good, controlling it is even better. *Guess Journal* runs upbeat stories about the jeansmaker. Benetton's *Colors* runs the same kind of controversial art that helped build the retailer's image around the world.



sonal products. They are looking for uniqueness, for things that are not the typical, average, familiar, mass-produced product that we've had around for so long," says Riney. "People are responding by creating these sort of fictional histories and fictional traditions."

Sometimes, too, companies adopt a new identity for the same reason people go into the witness protection program: The original ID has become bad news. That's what drove General Motors Corp. to dissociate itself from its innovative offspring, the Saturn. Because Detroit in general has suffered from a reputation for shoddy cars, sleazy dealers, and lousy service, GM set up a Saturn plant in Tennessee and hired Riney to package it as a small-town enterprise, run by folks not terribly unlike Frank and Ed.

Whether Saturn customers are buying into better service and cars or buying into Riney's vision of small-town values, their cult-like devotion is the envy of other marketers. Two years ago, 44,000 of them trekked to Tennessee for a "reunion." Last year, Saturn was the nation's fifth-best-selling car.

Knowing that consumers are increasingly cynical about the claims in traditional ads, other advertisers have tried to ignite, appropriate, or imitate grassroots trends and fads. "When you're looking at younger consumers, you can't tell

LET'S TALK
ABOUT THE SEAT YOU'LL SOON
BE ON THE EDGE OF.

*T*HE DRIVER'S SEAT in the Acura 3.5RL is so luxuriously comfortable, the natural inclination is to settle back, let the adjustable lumbar support go to work, and relax. Its hand-gathered leather is exceptionally soft to the touch, thanks to a special curing process. There are computer-designed springs that absorb extraneous vibration. Even a two-position memory.

It's a level of refinement equaled only by the other appointments found in this automobile: burled walnut trim, a CD audio system, and elegant instrumentation. All encompassed by a whisper-quiet cabin.

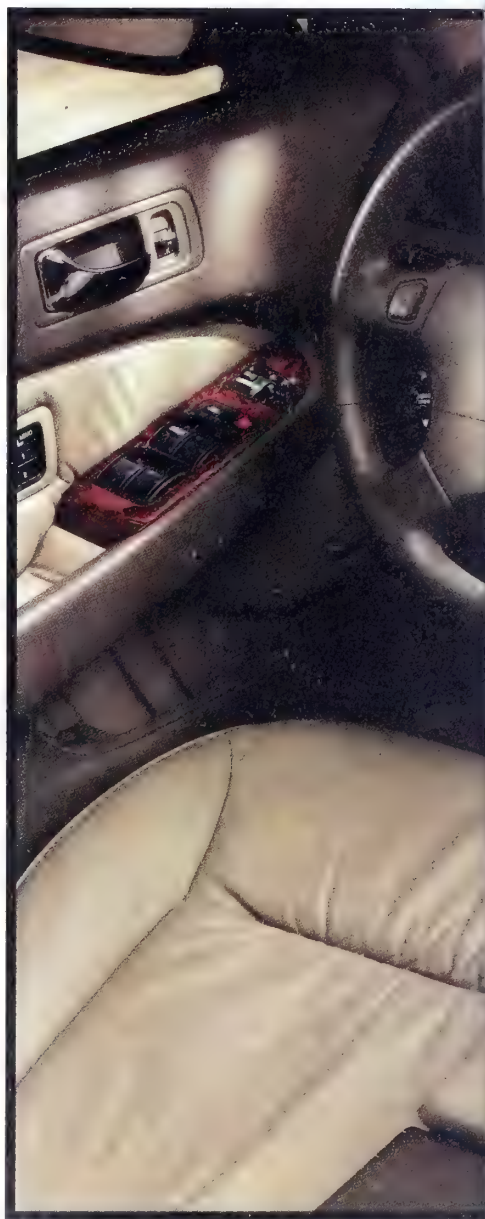
Punch the accelerator, however, and any notion of lazy tranquility goes right out the window. For under the hood lies the spirited wallop of a 3.5-liter V-6 which, in combination with a finely tuned suspension, translates into a ride that will keep you on the edge of, well, you know.

Which isn't to say you'll never get the chance to sit back and enjoy this seat simply for what it is. Of course you will. Like when you're at a stop sign, for example. Or waiting for a light to change.



To find out more information, call 1-800-TO-ACURA.

ACURA





THE NEW ACURA 3.5RL

- 3.5-LITER, 210-HORSEPOWER, V-6 ENGINE
- STEERING WHEEL-MOUNTED AUDIO CONTROL
- ELECTRONIC TILT AND TELESCOPING STEERING COLUMN
 - AUTOMATIC CLIMATE CONTROL SYSTEM
 - POWER MOONROOF WITH TILT FEATURE
- HEATED FRONT SEATS* WITH MEMORY FEATURE
 - 4-SPEAKER PREMIUM SOUND SYSTEM

them what's cool," says Ric Militi, head of integrated communications at ad agency Lois/EJL in Los Angeles. "Generally, if it's advertised, it's immediately uncool."

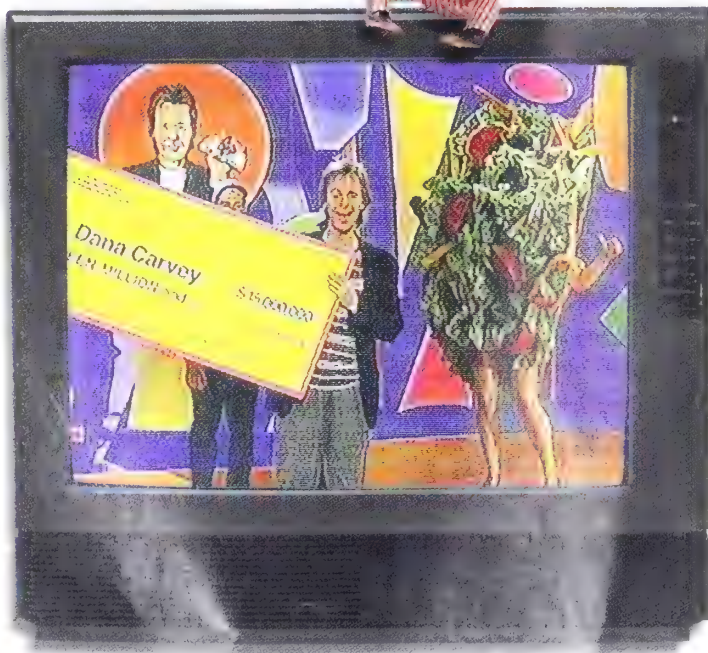
That's why marketers work hard to make promotions look as unplanned as possible. Militi spotted an opportunity last fall when Spelling Entertainment Group Inc., alleging trademark infringement, forced bar owners to stop hosting *Melrose Place* parties. The parties were springing up spontaneously at bars around the country on Monday nights when the prime-time soap opera aired. Militi quickly bought a license from Spelling on behalf of Hiram Walker & Sons' Kahlúa Royale Cream. He followed up each cease-and-desist letter the producer sent to bar owners with a marketing kit for a Spelling-sanctioned Kahlúa-sponsored party, complete with life-size cutouts of the cast, *Melrose* trivia, and plenty of Kahlúa knickknacks.

Other advertisers seek out chances for noncommercial commercials on TV and in the movies. Owning a piece of the show is one way to sneak aboard. Anheuser-Busch Co. owns a small stake in *Second Noah*, a syndicated series. The payoff? Exposure for Busch Gardens Tampa Bay, where the show is shot. Increasingly, networks are happy to cater to adver-

Cover Story

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YIKES! INFOMERCIALS WITH COMMERCIALS

Infomercials aren't just the el cheapo late night affairs of yesteryear. Now they look like regular TV—right down to the commercials. Paramount advertised its *Duchman* cartoon inside a 30-minute commercial for a music anthology, also made its own infomercial last year to promote the launch of a new TV series.

Advertisers who want a bigger role. Witness Capital Cities/ABC Inc.'s short-lived *Dana Carvey Show*, which tried selling title sponsorships each week. The ex-*urday Night Live* comic lampooned sponsors' products as part of the night's entertainment. The strategy backfired. Week One, when Pepsi's Taco Bell found it didn't have stomach for Carvey-style humor, which included calling himself a "whore" for the sponsor. Although Carvey seemed to tone down the gags after the first week, there were three other sponsors, all Pepsi beverages, before the gimmick was abandoned. The show was canceled in April.

CAMEO HEAVEN. Sometimes, telling the show from the commercial is even harder. Elizabeth Arden Co. didn't pay Elizabeth Taylor's

appearances on four CBS comedies earlier this year. But the exposure for the star's new Black Pearl perfume from Arden was a marketing coup. The plot of each show was written around Taylor, playing herself, and her perfume brand. Was it marketing? Entertainment? Who cares? Arden got better exposure than ad-budget money could buy, and CBS's ratings for the heavily hyped evening were way up. "From a marketing standpoint, it was brilliant," says Betsy Frank, executive vice-president of Zenith Media. "It was as seamless as you can get."

While shows have started looking more like commercials, commercials have started looking more like shows. Take the new breed of infomercials, those 30- or 60-minute ads that once were the domain of the pulpy schlocky. Now, solid-gold marketers from Microsoft to Ford to Eastman Kodak are airing them. Gone are the tacky sets and lousy production values. These segments now mimic talk shows or even newscasts. Time Inc.'s infomercial for its *Rolling Stone* "Sound of the '80s" music collection even managed to sell time to yet another advertiser. Halfway through the 30-minute

NO LAUGHING MATTER

The dancing taco is part of a song-and-dance number spoofing Taco Bell, the first title sponsor on the *Dana Carvey Show*. Carvey built each week's sponsor into the gags. But the jokes were too raw for Taco's parent, PepsiCo. Despite the exposure, it bailed out of the show.



HOW TO CARRY 27 BILLION POUNDS AND STAY FAST ON YOUR FEET.

A billion pounds here. A billion pounds there. You might expect all that tonnage to slow down an operation. Not The CF Companies.

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WE PUT YOU MILES AHEAD





CONCRETE PROPOSAL

There's no such thing as an ad-free zone. Marketers that want their ads to stand out look for spaces far from the glut of ads clogging the usual media. The goal: an unconventional site that gets lots of traffic. The company stenciled an arresting message on city sidewalks.

become infested with brand name goods, such as product placements start to lose their punch. "The problem with marketing that doesn't identify

self as marketing is that consumers catch on and it loses impact," says adman Bond. "It's not in the movie because such a cultural icon, but because someone paid for it."

That's why marketers work so hard to make the gap between ad and entertainment as smooth as possible. When it comes to truly smooth melding of the two, no one matches Martha Stewart, queen of the domestic arts, who combines a potent promise that housework can be glamorous with unparalleled media savvy. Her empire, which includes magazines, books, TV shows, and a nascent mail-order business, perfectly merges the Martha editorial message with the Martha marketing message. When Martha shows us how to make a pastry on television or how to tend lilacs in her magazine, that's information, but it's also an extended look at a lifestyle.

breathing logo. Stewart so completely embodies her brand that virtually everything she does, whether it's a commercial for American Express Co. or a guest spot on *Entertainment Weekly*, brings in new customers for Brandy. Martha.

Stewart may be the best indicator of where advertising is headed as it converges with the editorial content on our TV screens, in magazines, and on our computers. Clearly, Stewart's fans, who are legion, want what she is selling. But what if all entertainment and information came entwined with a brand name and every human encounter were mediated by a commercial sponsor? Advertisers say they only run the commercials that bring in customers. Stop buying, and they rethink their campaigns. Maybe.

But in a world weary of their incessant sales pitch, you have to wonder if there's anything that's not for sale. If you find it, enjoy it while it lasts—before somebody decides to sponsor it.

By Mary Kuntz in New York
Joseph Weber in Philadelphia,
Heidi Dawley in London

Cover Story

pitch, a cartoon character breaks into the program. In essence, the appearance of Paramount Television Group's Duckman is a paid message inside another paid message.

Even Broadway producers are getting into the sponsorship act. When *Big, the Musical*, opened on Broadway in April, toy seller F.A.O. Schwarz got co-producer billing—and marketing mileage that extends far beyond the credits.

The play's sets recreated the Fifth Avenue store for a crucial scene. Meanwhile, the store recreated the sets. Visitors at either location could buy plenty of Schwarz-marketed *Big* merchandise. "This has not been an attempt to overtly aggrandize F.A.O. Schwarz," says John H. Eyler, president of Schwarz. At least one critic at the Detroit tryout disagreed, lambasting the show for blatantly plugging the toy store. Some of the most adulatory bits were cut before the New York opening, but the producers said the changes had nothing to do with downplaying Schwarz.

As movie screens and other venues

FAKE REAL LIFE

Beware of a spontaneous product endorsement, especially for something you've never heard of from people you don't know. Hiram Walker & Sons hired cool-looking actors to hang out in bars and talk up a new drink made with an aging brand, Hennessy cognac.



body has a longer walk to school.

Motorola is proud to sponsor the 1996 Motorola Western Open, benefiting the Evans Scholarship Foundation. This year, because of the Evans Scholarship, over 840 caddies from across the country will get where they want to go. To college.

Remember to tune in to the Motorola Western Open on USA Network, July 4 and 5, and CBS, July 6 and 7, 3-5PM, CDT.



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WHERE LBO MEANS 'LET'S BE OFFBEAT'

Hicks Muse's unusual approach puts it in the top tier

At first glance, the tiny division of chemical giant DuPont Co. was not an operation to quicken the pulse of a dealmaker on the prowl. The unit was in the ho-hum business of producing electrical connectors, sockets, and cable assemblies. But to the Dallas leveraged-buyout firm Hicks, Muse, Tate & Furst Inc., it seemed a terrific opportunity. First, Hicks Muse had a St. Louis management firm, Mills & Partners Inc., study the division. Mills's conclusion: The division's earnings would be boosted considerably as a stand-alone company. Hicks Muse proceeded to fork over \$370 million to DuPont in March, 1993, renamed the unit Berg Electronics Inc., and replaced its general manager with James N. Mills of Mills & Partners. Then, Hicks Muse shelled out a further \$135 million for Berg to buy six more related companies.

The result: Berg zoomed from being the seventh-largest electrical supplier in 1993 to No. 4 in 1995. During that time, earnings nearly doubled, to \$113 million. Last March, Hicks Muse took Berg public at 21 a share. It now trades at 25, a hefty gain over the \$4.11 Hicks Muse originally paid for the stock.

Investments like Berg have made Hicks Muse one of the most successful LBO outfits in the country. And they have made a bundle for chief executive Thomas O. Hicks, his firm, and its in-

vestors. Annual net returns, after fees, on over \$1 billion in funds, is about 25%, say investors. "That's a terrific number if they can get it consistently," says Steven P. Galante, editor of *Private Equity Analyst*, a Wellesley (Mass.) newsletter. "I would put them in the top tier of LBO firms." The industry averages net returns of 16%, he adds.

BREW-HA-HA. What sets Hicks Muse apart from competitors? Short answer: The firm has an unusual approach to the deal business. Hicks Muse pioneered the now common "buy-and-build" strategy of using a core acquisition as a platform to acquire related businesses. The add-ons create value for investors by allowing the enlarged company to go public or be sold at a higher price. Hicks Muse also relies heavily on management firms to operate about half the companies it owns. Very few LBO firms hire outside managers for their operations. Hicks argues that this approach helps his firm size up acquisitions and get management in place fast. "Management affiliates allow us to do deals that other buyers can't do," he says.

The management-affiliate strategy isn't foolproof. Hicks Muse's 1994 purchase of G. Heileman Brewing Co. is expected to cause a \$54 million hit for the firm when Stroh Brewery Co. buys it out of bankruptcy this July. And another investment, Healthco International



al Inc., a Boston dental supply company, went bankrupt in 1993.

Now, with high LBO returns becoming increasingly difficult to come by, Hicks Muse is embarking on an ambitious diversification strategy that is taking it afield from what it knows best. Last year, it committed \$25 million to Stratford Capital Partners to invest in other companies. Stratford is a small-business investment company (SBIC), an entity subsidized by the Small Business Administration. Hicks Muse also purchased \$270 million in Olympus Real Estate Co. in 1994. And with two other partners, Hicks Muse has created TCW/Cree-

FROM HATS TO CHOCOLATE, AN ECLECTIC MIX AT HICKS

Publicly Traded Investments

	DATE ACQUIRED	TOTAL INVESTED	CURRENT VALUE*	RETURN**
BERG ELECTRONICS	MAR. 1993	\$35	\$205	72%
CHANCELLOR BROADCASTING	JAN. 1994	47	184	91
LIFE PARTNERS GROUP	MAR. 1990	24	148	46
MORNINGSTAR GROUP	MAR. 1991	11	49	42

* Based on 6/10/96 stock prices

** Annual rate of return

Private Investments

G. HEILEMAN BREWING Jan. 1994 Spent \$390 million on regional brewer. Hicks Muse invested \$61 million and is expected to lose \$54 million.

GHIRARDELLI CHOCOLATE Apr. 1996 Bought company for \$65 million.

HAT BRANDS Sept. 1992 Dallas maker of Stetson, Montana Silver-smith, and Resistol hats. Capitalization: \$206 million.

HEALTHCO INTL. May 1991 Bought dental supply company; in bankruptcy since 1993. Hicks Muse expected to lose \$53 million.

HEDSTROM Oct. 1995 The nation's largest maker of children's outdoor swinging sets and toy balls. Capitalization: \$90 million.

DATA: HICKS MUSE; BUSINESSWEEK



BORN TO BUY THINGS: Hicks (front) and his partners pioneered the now-common "buy-and-build" strategy

zanine Partners, a \$335 million fund, finance non-Hicks Muse deals. "I 't know of any other firm" that has ersified to such a degree, says ante. "That's important for building a petitive edge."

om Hicks, 50, has proved a master reating competitive edges. A 6-foot, ch Texan who just plunked down million of his own money to buy Dallas Stars hockey team, he made first big LBO splash in the mid-'80s h buyouts of Dr Pepper and Seven- with then-partner Robert B. Haas. five years, they did \$4 billion worth deals, turning \$88 million of investors' rey into \$1.3 billion, says Hicks. The tners split up in 1989 over differ- es about how to fund their deals. as declined comment. Hicks immedi- ly teamed up with John R. Muse, a tential Securities Inc. banker and S. Air Force Academy graduate. Oth- partners include Charles W. Tate and k D. Furst, as well as three others. Among Hicks's most valuable assets his contacts, say many of his in- tment bankers and investors. "Hicks i rainmaker," says Robert L. Zobel, estment director for the State of consin Investment Board, which has million invested with Hicks Muse. Last December, for example, one of ks Muse's affiliated managers and

its insurance broker learned from the CEO of San Francisco's Ghirardelli Chocolate Co., the world's largest, that the company was for sale. Hicks Muse quickly engineered a \$65 million buy-out. When the deal was announced in March, few in the industry were even aware that the firm was on the block. "Ghirardelli could have turned into a bidding war or an opportunity we didn't even get to see at all," says Muse.

The firm's best score has been in radio, something Tom Hicks knows something about: His father bought small radio stations in the South. During his high school years in Port Arthur, Tex., Hicks worked as rock 'n' roll deejay "Steve King" at one of his father's stations.

In 1993, Hicks Muse created Chancellor Broadcasting Co. as a radio buy-and-build operation. Chancellor bought its first station in January, 1994. Last February, it paid \$385 million for 19 stations. That made Chancellor the third-largest radio-only broadcast group in the country, operating 33 stations in 15 major markets. The same day, Hicks Muse took Chancellor public at 20 a share. The stock now trades at 25%. Hicks Muse investors had paid only \$6.65 a share. Now Hicks Muse is building another radio empire, Capstar Broadcasting Partners, to buy AM and FM stations in midsize markets.

The Heileman deal was perhaps the firm's worst miscalculation. When Hicks Muse yanked the La Crosse (Wis.) regional brewer out of bankruptcy in January, 1994, for \$390 million, it seemed like a steal. Heileman was saddled with \$247 million in debt from a failed \$1.3 billion LBO by Australian financier Alan Bond. Sales of its largest brands, with the exception of its Colt 45 malt liquor, had been declining for three years. Hicks Muse, though, thought it could nurse Heileman's regional beers into profitable brands.

PRICE-WAR CASUALTY. The brutally competitive, no-growth beer market was bad enough. But Hicks Muse made matters worse by hiring Turner & Partners Inc., a management firm with no previous experience in the beer industry. Turner tried to expand Heileman by launching 150 new products and taking the brewery's Henry Weinhard's label national on a very limited budget. Both experiments proved wildly overambitious. Facing shrinking sales, Turner started a price war in the malt-liquor market, where Heileman made most of its money. "Before we knew it, we had given away 25% of our cash flow," says Hicks.

After a loss of \$37 million in 1994, compared with income of \$17 million in 1993, Hicks Muse replaced Turner with a soft-drink industry veteran. But in 1995, Heileman suffered a \$64 million loss and missed its debt payments. Hicks Muse plans to sell Heileman to Stroh's for an estimated \$290 million. Turner declined comment. "Hicks Muse had people running the company who didn't understand the business," says Robert S. Weinberg, an independent industry analyst. "No one in the industry was surprised when they failed."

Hicks is now busy trying to raise \$1.5 billion for his third fund. Despite the frothy stock market and deal prices, which have sidelined many LBO players, the firm has stayed busy. Since January, 1995, Hicks Muse has acquired seven companies. It also paid \$115 million for an 18.6% minority stake in Marcus Cable Co. And it's selling insurance holding company Life Partners Group Inc. to Conseco, an Indiana financial services company, later this month in an \$875 million deal. And Hicks Muse is looking toward Latin America for deals.

Hicks Muse still has to prove that its skills in U.S. LBOs are transferable to its new endeavors, from Latin America to small business. Hicks and his investors are betting they are.

*By Stephanie Anderson Forest
in Dallas*



PANIC ATTACK

Legal and business troubles pile up for ICN's chief

JULY 1992 ICN Pharmaceuticals CEO Milan Panic appointed Prime Minister of Yugoslavia.

FEBRUARY 1993 Panic ousted, returned to ICN; fights and wins proxy battle.

NOVEMBER 1994 Stock sale garners Panic \$1.2 million, provoking insider-trading probe.

JANUARY 1995 Former employee sues ICN and Panic for sexual discrimination and harassment, renews paternity action.

JUNE 1995 Panic and ICN sued by shareholders for trading on inside information.

FALL 1995 SEC begins investigation of Panic's trades.

MAY 1996 ICN says grand jury is investigating trades. IRS demands \$951,077 in back taxes and penalties from Panic and wife.

DATA: ICN, COURT RECORDS, BUSINESS WEEK

PANIC DISMISSES THE ALLEGATIONS, SAYING THAT "SOCIETY IS PRO-LAWSUIT"

CONTROVERSIES

MILAN PANIC MAY BE STARTING TO SWEAT

Shareholder suits and fed investigations dog the ICN honcho

Few men have worked harder than Milan Panic to create a world-class image. A Yugoslavian immigrant who started ICN Pharmaceuticals Inc. in 1959 with \$200 and some used machinery, the 66-year-old chairman and CEO of the \$508 million drug company today plays on the world stage. Photos line the wall of his Costa Mesa (Calif.) headquarters chronicling meetings with the likes of Bob Dole, Bill Clinton, and China's Li Peng, taken during his eight months as Prime Minister—from July, 1992, to February, 1993—to stabilize his war-torn homeland.

But a far different image of Milan Panic is emerging. Since his return from Belgrade, the ICN chairman has been hit with a flurry of shareholder lawsuits, a Securities & Exchange Commission investigation, and a subpoena for documents by a U.S. District Court grand

jury. The actions all concern possible insider trading related to the timing of a November, 1994, sale of company stock worth \$1.2 million.

A separate \$315 million class action accusing Panic and the company of making false and misleading statements about the usefulness of Virazole, ICN's star drug, is scheduled for trial this July. Meanwhile, the Internal Revenue Service has accused Panic and his wife, Sally, of failing to pay proper taxes on an energy limited partnership and a pair of Budget Motels of America they own in California. The bill: \$951,077. As CEO of ICN, Panic makes \$535,000 a year, a stipend he garnered even when he was Prime Minister of Yugoslavia.

Potentially most embarrassing is a decision that may come between now and July 4 on a paternity suit filed by Debra Levy, a former secretary, who

claims Panic fathered her son. She alleges sexual harassment and claims that after she ended her long-term relationship with Panic, he forced her to resign.

Panic dismisses these allegations, attributing them to malcontents and saying that "society is pro-lawsuits." The insider-trading charges claim that Panic sold \$1.2 million of his own ICN stock at a time when he knew that an action by the Food & Drug Administration to permit Virazole to treat hepatitis C was not going to be approved. Investors said they were not told of the disapproval until three months later. ICN's board cleared Panic of wrongdoing a year ago. Panic is fighting the ICN's outside lawyer, Arnold I. Burns, former Deputy U.S. Attorney General under Ronald Reagan, is confident that all litigation will be resolved in Panic's favor. "The company has superb defenses to the [civil] claims," Burns says. The SEC investigation is now "quiescent," he adds, and the possibility of a grand indictment is "highly unlikely."

Panic has often had run-ins with regulators and shareholders. In 1977 and 1991, without admitting or denying it, he signed consent decrees to settle charges of releasing misleading statements. One of the class actions asserts that ICN misled investors about Virazole's usefulness in treating a variety of viruses and illnesses. More recently,

ch acquired Galenika, Yugoslavia's est drug manufacturer, in 1991, pubed Galenika's launch of Eli Lilly & s Prozac in Yugoslavia. It also said nika would be selling Prozac in Rus- under another name. Lilly says that's curate, claiming the drug has been lable in Yugoslavia through Galenika more than four years. And it says e's no deal for ICN to sell the drug in sia. "We don't know where that press ase came from," says Lilly spokes- an Victoria Murphy. ICN's general sel says wartime sanctions prevent- arketing of the drug in Yugoslavia that Russian rights were granted. There needs to be a new chapter in s development," says Eugene Melnit- to, head of research at Dallas-based ipal Financial Securities and a for- ICN executive. "The baggage Milan accumulated over the years is now ishing the company fundamentally."

IOCRE. While Panic wrestles with e problems, some of ICN's funda- tals are improving. Strong business astern Europe, which accounts for of its sales, helped revenues rise last year. But that has been offset the company's long-term mediocre orrmance in the U.S. Further, since ounding 37 years ago, ICN has had one big hit, a compound called rib- in, which it markets as Virazole. Ap- ved for a variety of applications lwide, Virazole is authorized for one major application in the huge t. market: the treatment of hospital- children with respiratory syncytial s, a common ailment. The drug is ensive and "probably not useful in majority of cases," says Dr. Daniel Notterman, a specialist in pediatric nsive care at New York Hospital a member of the American Acade- of Pediatrics committee on drugs. orts to get the drug approved for in- nza, hepatitis C, and AIDS-related dis- es have not panned out.

anic has taken steps to address some CN's problems. ICN has hired a re- ted new chief of research, Devron rettt, from Glaxo Wellcome, and nised to increase R&D spending from than 3% of annual sales to closer to 19% industry norm. Although new gs are years away, ICN has a lucrative eement with Schering-Plough Corp. to lore a promising combination of rib- in and Schering's drug alpha inter- m for treatment of hepatitis C.

I think Panic will be there for a long e," says Seth Glickenhau, whose any, Glickenhau & Co., holds hun- ds of thousands of shares of ICN. "I o think that's unfortunate." Other in- tors likely share those sentiments.

By Nanette Byrnes
in Costa Mesa, Calif.

INSURERS

INSURANCE GETS SEXY

The stodgy business is rife with hot IPOs

APAC Teleservices Inc., whose sales have doubled in the past three years, went public last year at a price of 16, then soared to 88 before splitting 2 for 1 in May. SS&C Technologies Inc., whose revenues tripled in the past three years, initially filed in the 9-to-11 range but came out at 19. Riscorp Inc. also rolled out at 19 and traded as high as 24, a heady 36 times expected 1996 earnings.

Are we talking about hot new Web browsers? Digital animators? Companies with innovative telecom linkages? Nope. These companies, believe it or not, are in insurance.

Given the industry's mediocre returns and growth rates, it may seem curious to see investors chasing these initial public offerings. "The macro numbers in insurance are kind of blah," says John B. Clinton, senior vice-president at Conning & Co., a Hartford consulting and investment firm. Yet insurance is one of the few corners of the market where good values remain. Some \$3.2 billion was raised in insurance IPOs in 1995, a figure likely to be surpassed this year.

It's slow growth among giants that makes small outfits look hot. Consider Riscorp, a Sarasota (Fla.) company that takes a managed-care approach to workers' compensation insurance. Its revenues have risen nearly tenfold, to \$166 million, since 1990, and analysts think profits will grow at a 30% annual rate for the next five years. Following a pattern common among IPOs, Riscorp has

slipped below its offering price. Now at 16%, or 24 times 1996 earnings, it's cheap if its forecast growth rate holds up.

Also seemingly cheap is IPC Holdings, a Bermuda reinsurer. It's a startup but with a big investor: American International Group Inc. has a 25% stake. Reinsurance companies, which help underwrite other insurers' risks, have boomed in recent years because of the natural catastrophes that have drained the reserves of many primary carriers. Now at 20%, IPC is 10% below its IPO price and sells for a rock-bottom six times expected 1996 earnings.

UMBRELLA DEAL. Not all the action is in small companies. The IPO boom is also fueled by industry restructuring, which is creating a leaner breed of big companies. So far, the year's biggest insurance IPO was the April offering of a 10% stake in Travelers/Aetna. The new property-casualty insurer took shape last year, when Travelers Group Inc. acquired Aetna Life & Casualty Co.'s P&C unit for \$4 billion. Travelers/Aetna, which went public at 25 and raised \$886 million, now trades at 26%. Another big outfit with a deal in the works is AXA. The French insurer expects to raise \$200 million on the hot U.S. stock market with an offering of American depositary receipts.

Some of the best IPOs provide services to the industry. APAC Teleservices, a telemarketing company, gets a good chunk of its revenues from insurance carriers that hire it to do cold calling. SS&C Technologies sells investment-management software to leading insurers.

Still, Allan W. Fulkerson, who manages Century Shares Trust, a mutual fund specializing in insurance stocks, advises caution in playing the insurance IPOs. "I'd just as soon let the euphoria die down," he says. With more IPOs and industry restructurings in the pipeline, investors can afford to be choosy.

By Tim Smart in Hartford



A SPATE OF OFFERINGS

DEALS ANNOUNCED

COMPANY	AMOUNT MILLIONS	ESTIMATED SHARE PRICE
AXA	\$200	28
FBL FINANCIAL	78	19½
FPIC GROUP	41	10-12

DEALS COMPLETED

COMPANY	AMOUNT MILLIONS	IPO PRICE	RECENT PRICE
TRAVELERS/AETNA	\$886	25	26%
IPC HOLDINGS	238	22	20½
RISCORP	190	19	16½

DATA: CONNING & CO., BLOOMBERG FINANCIAL MARKETS

By Gary Weiss

THE FLIMSY CASE AGAINST JOSEPH JETT

In the annals of Wall Street scams, Orlando Joseph Jett holds a special—and contemptible—place. This former Kidder, Peabody & Co. bond trader allegedly masterminded \$340 million in phony trades from 1991 to 1994. So badly was Kidder tarnished that its name was dropped when its assets were sold by General Electric Co. to PaineWebber Inc. last year. According to the Securities & Exchange Commission, which is wrapping up administrative proceedings against Jett in New York City, the 38-year-old trader was a cunning flimflam artist.

There is only one thing wrong with this picture: There's an awfully good chance that Joseph Jett is an innocent man.

If that sounds ludicrous, it's understandable. For two years, Jett has been pilloried by his former employers and the SEC. His accusers say the former trader secretly abused an "anomaly" in Kidder's trade-accounting system that recorded "phantom" profits from "stripping" and reconstituting Treasury bonds into their interest and principal components. He manufactured phony profits, they say, under the noses of his bosses—and was so good at it that Kidder proudly named him its Man of the Year in early 1994. Even now, says Kidder general counsel John Liftin, "there's no evidence that he has anything resembling a defense."

But Jett's defense is substantial. He claims that he was using—not abusing—Kidder's computer system and was singled out for blame when the accounting system was changed. Evidence produced at his trial makes a persuasive case that he conducted his trades openly—and even disclosed them to Kidder's internal auditors. And that undermines one of the central tenets of the SEC's case: that Jett was deceptive.

To prove securities fraud, the SEC must demonstrate intent—"scienter," as lawyers call it. As defined in one U.S. Supreme Court ruling, that's a "mental state embracing intent to deceive, manipulate, or defraud." The

key word is deceive. But documents introduced at the SEC's proceedings against Jett seem to favor him on this crucial point:

■ **"Red Books."** Jett's trades were recorded by Jett and other traders in large ledger books, or "red books," that he kept in plain view on his desk. They were available for anyone to peruse during Jett's frequent absences from the desk. The books un-



ABOVEBOARD: Jett conducted trades openly at Kidder

dercut the theory that Jett was acting stealthily.

■ **Auditors.** Persuasive evidence indicates that Jett cooperated with Kidder's internal auditors during routine audits in 1993—hardly the behavior of a scamster. According to interview notes between auditors and Kidder lawyers, which were produced as evidence in the SEC proceedings, auditors said his trading desk "did not try to hide anything, and in fact Jett was more helpful than most other managers." A chart prepared by Kidder auditors in July, 1993—eight months before the scandal broke—showed that Jett engaged in a high volume of "forward transactions... one to three months." That may indicate the auditors were aware of Jett's trading strategy. Liftin says the auditors were inexperienced and did not understand Jett's trading.

■ **The Bernstein Notes.** David Bern-

stein was assistant to Edward A. Cerullo, Kidder's fixed-income chief. According to notes of an interview with lawyers for Kidder, Bernstein said that "Kidder can't deny that plus people knew that forward trade with Fed took place. Issue is [if] it had P&L [profit-and-loss] effect." Cerullo's notes record him saying they were "not really false profits." Bernstein testified at the hearing that he did

not recall making those comments. The lawyer for Kidder who took the notes, Lawrence Portnoy, says the comment on profits was Bernstein's account of Jett's view of the subject. Jett testified that Bernstein was stating his own view on the validity of the profits.

■ **"Inventory Committee."** Minutes of a September, 1993, meeting of Kidder's inventory committee, which rode herd on Kidder's assets, were introduced at trial. Cerullo is quoted as saying his department would move assets off the balance sheet "such as by doing trades with forward settlements." Jett's lawyer, Kenneth E. Warner, says this reference to Jett's trading. However, Cerullo has denied knowing about Jett's trading

until March, 1994.

Liftin says that "while a number of people may have been aware of the stripping and reconstituting activity, no one else at the firm was aware that the trading was producing profits that had no economic reality." But that claim wages war with common sense. If Jett was truly a secret profiteer, why did so many people know what he was doing? Why did he cooperate with auditors and keep a handwritten record of his trading for all to see? Why did he keep all of the money he received in bonuses, \$5 million on deposit at Kidder—where it was swiftly frozen when the scandal broke? Joseph Jett is nobody's champion for Man of the Year nowadays. But did he really commit securities fraud? Don't bet on it.

Weiss has covered numerous Wall Street scams over the past decade.

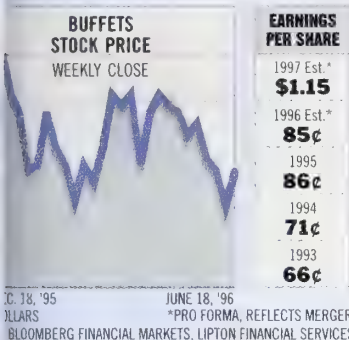
GENE G. MARCIAL

BUFFETS TO MAKE OUR MOUTH WATER

When Buffets (BOCB), which runs 250 self-service restaurants, announced June 4 that it was acquiring its rival—HomeTown Buffet—shares of both companies slipped. But industry observers think the deal will be good for both.

One investor blames the decline on the company's lack of Street following: It has provided any investment-banking business since it went public in 1985. The investor ascribes it to expect-

PUZZLING LOSS OF APPETITE



ons of an earnings dilution. But Lipton, who heads Lipton Financial Services, an affiliate of Axiom Management, is upbeat. "It's a change made in heaven," he says. Lipton thinks Buffets has become "even more undervalued" as a result of the acquisition.

Now at 12, shares of Buffets, whose restaurants are mainly in the Midwest, could more than double in a year or so if the deal bolsters sales, earnings, and cash flow, says Lipton. The merged company will be the nation's 25th-largest company and the largest buffet-style outfit with Old Country Buffet restaurants in 32 states. HomeTown operates 93 restaurants, mainly on the West Coast. HomeTown's shares, which fell from 15½ to 13½ when the deal was announced, closed at 13½ on June 18. The big deal about the acquisition, says Lipton, "is Dennis Scott," now HomeTown's chairman—and co-founder of Buffets. He left Buffets five years ago to run HomeTown. Under his stewardship, HomeTown grew to become a premier restaurant, notes Lipton, while Buffets' profit margins have narrowed.

With Scott rejoining Buffets as chief operating officer, Lipton expects he'll bolster Buffets' top and bottom lines. Next year, Lipton figures Buffets' sales should climb to nearly \$1 billion, with cash flow of \$2 a share and earnings per share of \$1.15. For this year, Lipton expects the merger will lift Buffets sales to \$794 million, cash flow to \$1.66 a share, and earnings to 85¢.

Analyst Michael Mueller of Montgomery Securities says the acquisition gives Buffets an immediate presence outside the Midwest.

KELLEY OIL FINDS ITS WHITE KNIGHT

Three years ago, Kelley Oil & Gas (KOGC) was a high-flying stock trading in the 30s—and a favorite target of the short-sellers, who saw it as a badly managed company with dwindling reserves, huge debt, and soaring costs. Oil investor Alan Gaines was one of those who shorted the stock—as it fell to 6 in early 1995. By December that year, Kelley had plunged as low as 1, and the Houston oil-and-gas exploration company came close to filing for bankruptcy. Now, some pros, including Gaines, are bullish. The stock has rebounded to nearly 3. What's going on?

"The picture has changed—very much for the better," notes Gaines, president of Gaines Berland, which specializes in energy plays. The best thing that has happened to Kelley is John Bookout, president of Contour Production, who in February bought 48 million newly issued shares at 1 apiece, representing 49.8% of Kelley's voting stock. Founder David Kelley was ousted, and Bookout was named chairman, president, and CEO.

Bookout has a rich background in the industry: He was president and CEO of Shell Oil from 1976 to 1988, when he retired. "Bookout brings an entirely new dimension of executive expertise, financing capability, and acquisition deals," says Gaines. He expects Bookout to expand reserves in Louisiana, pursue acquisitions, and beef up the balance sheet. Already, Bookout has cut losses in the first quarter to 8¢ a share, down from 28¢ last year, with cash flow turning positive.

Gaines figures cash flow next year will jump to 32¢ a share, up from an estimated 12¢ in 1996 and negative 78¢ in 1995. Last year, Kelley had a loss of \$1.65 a share. Gaines expects the loss

will narrow to 22¢ in 1996 and to 5¢ in 1997. The stock, he says, should hit 6 this year and 10 in 1997.

ALLIANCE: MAKING MICROSOFT MUSIC?

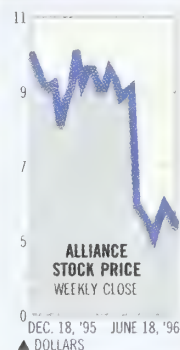
Shares of Alliance Entertainment (CDS) have yet to recover from the knockout blow Metromedia International dealt on Apr. 29, when it withdrew its \$685 million buyout bid for the largest independent U.S. wholesale supplier of recorded music. Shares of Alliance traded as high as 10 in early February—right after Metromedia announced the buyout pact. When it was called off, Alliance fell from 9 to 6. Now at 5, the stock is again a target, say some pros who insist a new suitor is "in the wings, now that the stock is flat on its back."

Says a New York money manager who is accumulating shares: "Joe Bianco [Alliance's chairman and CEO], who owns some 20% of the stock, is definitely looking for a buyer." He notes that, with Bianco having undergone preventive heart surgery in late April and with the music business finally staging a comeback, "it isn't hard to deduce that Alliance is for sale."

Bianco declined to comment on talk about another suitor. He also declined comment on rumors that Microsoft and Alliance have struck a deal in which Alliance will be the supplier of pre-recorded music for Microsoft's new virtual music store on the Internet. When Microsoft customers place an order, their selections will be delivered overnight. Whispers are the Microsoft-Alliance pact will be announced very soon. Alliance has 175,000 music titles in its warehouses. One investor expects sales from the Microsoft deal to hit \$200 million in a year. Microsoft declined comment.

Analyst Craig Bibb of PaineWebber notes that Alliance is trading at 9 times cash flow, compared with 11 for its peers. He sees the stock price hitting 9 in a year.

STILL REELING FROM A BLOW



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ACER: A GLOBAL POWERHOUSE

Taiwan's titan in PCs and peripherals aims to take the lead in the new market for intelligent consumer gear

Dixon Cheng steps out of his office in the cluttered executive suite at the Taipei headquarters of Acer Inc. and leads a visitor down a hall past cubicles where engineers sit hunched over projects. "It's right here," says Cheng, Acer's vice-president for information systems, as he squeezes around an awkward partition. An engineer seated on the floor hooks a simple white box to a television set and flicks it on. Three squares appear on the screen: "Basic Net," "Games," and "Windows." Using a remote control, he selects "Basic Net," and Acer's World Wide Web home page appears. Returning to the menu, he clicks on a different square, and Microsoft Corp.'s Windows 3.1 pops up.

The machine is called the Basic. Carrying a list price of \$499, it is one of many "information appliances" that Acer will unveil during a four-day bash to celebrate Acer Group's 20th anniversary. There will be prototypes of a \$500 video-game player, a \$200 children's personal computer, and wide-screen TVs. In the back room, Acer is working on everything from digital videodisk (DVD) players to video telephones. Says Acer Chairman and founder Stan Shih: "Our philosophy is to make it possible for everyone everywhere to enjoy these technologies."

By building the Acer Group into a \$5.8 billion global conglomerate, Shih, 51, has become Taiwan's answer to Intel Corp.'s Andrew S. Grove and Microsoft's William H. Gates III. Taiwan's dominant maker of PCs, peripherals, and chips, Acer has pushed

into markets from Malaysia to Mexico. Now, Shih aims to make Acer one of the top five computer companies in the world by 2000—a \$15 billion giant.

The plan? Move Acer to a new level—from a global force in PCs to a leader in a new market of intelligent consumer products. With the Internet PCs, smart TVs, and game machines now in the labs, Shih figures he can sustain annual growth rates of 25%—about 5 to 10 points more than the PC market alone will produce. By 2000, Shih is counting on having at least \$3 billion a year in revenues from new products. He also counts on further gains in markets from Moscow to Manila as well as growing acceptance for Acer gear in the key U.S. market.

COMING BATTLE. Acer has a running start. After years of frustration, it has broken out of the also-ran category in the U.S. market with inexpensive home PCs. And benefiting from Shih's global vision that has spawned 10 subsidiaries around the world, Acer now dominates many hot-growth emerging markets, where it gets 35% of its sales.

Acer also has one of the industry's most efficient manufacturing setups. A joint venture with Texas Instruments Inc. provides memory chips, and Acer factories build everything from PC motherboards and color monitors to keyboards and CD-ROM drives. The empire includes 39 just-in-time assembly



plants from San Jose, Calif., to Bay in the Philippines. Last year pumped out 4 million PCs, 1.7 million CD drives, 3.5 million monitors, and 1 million memory chips.

That global manufacturing muscle will come in handy in the new corner battle. Sony, Fujitsu, Compaq, IBM, NEC are equally intent on selling in the manner of electronic gadgets for a "digital living room."

Shih's biggest challenges, however, may be internal. First, he has to find a way to make money with the new products. Straddling the worlds of computers and consumer electronics may represent the worst of both worlds: products that require big investments in development but will have the razor-thin margins of TVs and VCRs. Acer is taking the risk: Its big consumer hit

ACER AMERICA
San Jose, Calif.
'95 REVENUES: \$1.44 Billion
PC MARKET RANK: #8
ACER OWNERSHIP: 100%

ACER COMPUTEC LATINOAMERICA
Mexico City
'95 REVENUES: \$3.1 Million
PC MARKET RANK: #1
ACER OWNERSHIP: 30%

ACER COMPUTER (Europe)
The Netherlands
'95 REVENUES: \$462 Million
PC MARKET RANK: NA
ACER OWNERSHIP: 100%

THE
WORLD
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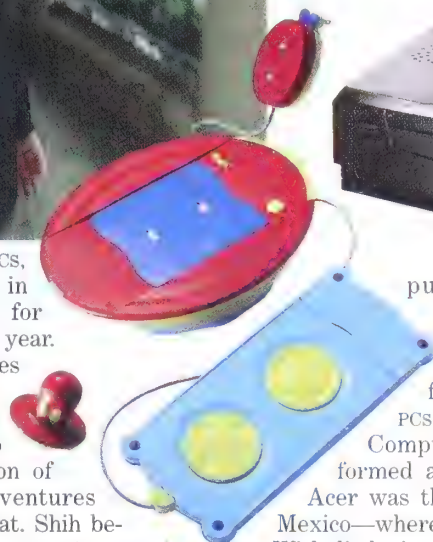
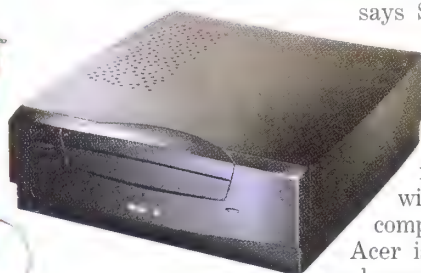
CHAIRMAN SHIH:

"Our philosophy is to make it possible for everyone everywhere to enjoy these technologies," he says.

In addition to wide-screen TVs and basic PCs, Acer's products include a children's computer and the Eden information appliance

the Aspire line of PCs, iced a 62% jump in ue, to \$1.4 billion, for America Corp. last year. he company concedes yet to make money e machines. other task is to keep s loose confederation of diaries and joint ventures ing to the same beat. Shih be-ving overseas units greater au-ty in 1990, and the move has been cess: Sales expanded sixfold be-1 1991 and 1995. PC shipments dou- to 4 million units, last year and hit 6 million in 1996—making Acer in the world.

D ALONE? One standout success een Mexico. Acer entered the mar-1 1989 using Computec, a distribut-1 focused on the small businesses ome-PC buyers that IBM, Hewlett-Packard, and the no-name clonemakers were missing. Com



putec invested heavily in mar- keting, includ- ing Mexico's first TV ads for PCs. By 1992, when Computec and Acer formed a joint venture, Acer was the top brand in Mexico—where it remains.

With little input from Taipei, Acer Computec Latinoamerica has revised tactics continuously—it has had little choice. After the 1994 peso collapse, for example, many companies tightened marketing, but Acer kept buying TV time and launched new multi-media models. "We had great flexibility to make decisions and respond quickly," says Armando Jinich, general director of Acer Computec Latinoamerica. The next moves: a thrust into the rest of Latin America and a plant to make components and subassemblies for the entire North American market.

Now, Shih, who owns 10% of Acer Inc., the holding company, has a radical decentral-ization plan: to spin off 21 units in the next four years. Acer's most profitable Taiwan manufacturing arms, \$1 billion Acer Peripherals Inc. and \$565 million TI/Acer, will become stand-alone companies. So will many foreign

marketing arms, such as Acer's U.S., Latin American, and European divisions. Acer Inc., the Taiwan parent that makes desktop and notebook PCs, servers, and motherboards, will retain big stakes in the offshoots.

But once subsidiaries start going public—Singapore's Acer Computer International did so this spring, and the Mexican and U.S. companies hope to follow within 18 months—their managers will have to answer to local shareholders, rather than Taipei. "After the units become more independent and local, it will be natural for investor pressure to push them to protect their own interests,"

says Shih. He's betting, however, that his engineers will come up with such irresistible designs that the affiliates will clamor for them.

Before he puts that theory to the test, however, Shih will have to see if these spin-off companies can stand alone. After Acer is broken up, the group can no longer use profits from units such as the chip plant and Acer Peripherals—which together accounted for 60% of the group's \$204 million in earnings last year—to subsidize losses overseas. "Acer has to be concerned about the marketability of these companies," says Taipei analyst Ben B.Y. Lee of Nomura Securities Investment Advisory Co.

KID STUFF. There won't be much to worry about if the overseas subsidiaries can repeat what Acer America has done—while turning a profit, that is. Just a few years ago, ill-fated acquisitions and inventory bottlenecks were sinking Acer America. But with new management, the wholly owned U.S. unit bet on a radically different TV-like design for its home PCs. The line was a runaway hit. Acer sold 300,000 Aspires in three months.

The Aspire's popularity inspired Shih's new consumer strategy, which is built on low-cost information appliances. With the Basic, Shih is hoping consumers will forgo the latest bells and whistles for a cheap machine that can't do much more than cruise the Internet. Acer is bringing the Basic in at \$500 by avoiding the cutting edge and eliminating some conventional parts. It's saving 60% over a hard disk by using Iomega Corp.'s "Zip" drive, a sort of high-capacity floppy disk drive, for instance. The standard model uses a TV for a display—a \$200 monitor is optional.

The next target is children. This fall, Acer will bring out Eden, its \$499 answer to Sony Corp.'s hugely popular PlayStation. Unlike the PlayStation, which uses proprietary Sony software, Eden is based on standard PC designs

ACER CIS INC. (Russia)
Moscow
'95 REVENUES: \$41.6 Million
PC MARKET RANK: #2
ACER OWNERSHIP: 90%

ACER COMPUTER INTERNATIONAL (Asia)
Singapore
'95 REVENUES: \$615 Million
MARKET RANK: #3
ACER OWNERSHIP: 63.4%

ACER GROUP
'95 SALES: \$5.8 Billion
EMPLOYEES: 15,352
MAIN BUSINESS: PCs, chips, peripherals

and will run Windows educational and entertainment CD-ROMs. It's also a word processor and plays audio- or videodisks. Acer expects to sell at least 200,000 Edens in the first year, mostly in Asia.

Acer is also using the Far East as a base for its assault on other consumer-electronics markets. In July, Acer plans to trot out a 28-inch high-resolution TV in Taiwan for \$1,100. A little later in the year, it will introduce a wide-screen TV that can double as a computer monitor. DVD players, high-speed CD-ROM drives, settop boxes for cable and satellite TV, and a multifunction machine that combines a fax, scanner, and color printer will be out next year.

HARDER PUSH. While Shih pushes ahead with his master plan, he will have to solve some short-term problems. One that could undermine the whole strategy is the volatile performance at Acer America. Shipment growth cooled off from 75% in the fourth quarter of 1995 to 25% in the first quarter, and inventory piled up. Even cutting the Aspire's price from \$2,200 last fall to around \$1,500 hasn't helped.

To rev up the U.S. unit, Acer is planning a national ad campaign with Hal Riney & Partners Inc. and expanded distribution. By the end of 1997, Acer hopes to move beyond chains such as Best Buy Co. and Incredible Universe, where it is the top-selling PC brand, to office supply and computer superstores. It's also renewing its push into the corporate market. The just-out Nuovo, a \$3,500 to \$4,000 notebook PC aimed at the corporate market, boasts a battery life of nearly nine hours.

Meanwhile, Shih is continuing his global push. Excluding Japan and Korea, Acer is No.1 in Asia—despite rising competition from Compaq Computer Corp. and IBM. Acer also is No.1 in Africa, No.1 in the Middle East, and No.2 in Latin America. Acer has even bested U.S. rivals in the former Soviet Union. Since arriving in late 1993, annual sales have zoomed from \$3.4 million to \$42 million.

What if Shih's new consumer gizmos don't catch on? As he sees it, Acer wins anyway. By building a low-cost manufacturing base and accumulating expertise in all digital technologies, Acer can still prosper the way it did before its PC success—as a behind-the-scenes supplier of components and systems sold by the big brand names. One way or another, Shih is determined to be a major player in the digital age.

By Pete Engardio in Taipei and Peter Burrows in San Jose, Calif., with bureau reports

ONLINE SERVICES

MONKEY BUSINESS IN CYBERSPACE?

AOL and rivals may face an FTC probe of billing practices

America Online Inc. has been on a wild ride this year. Spectacular subscriber growth boosted AOL stock from the mid-30s to a record high of 70 on May 7. But rising competition from Internet services and slowing growth has since plunged AOL stock to around 40.

There may be another dip on this roller coaster. BUSINESS WEEK has learned that regulators at the Federal Trade Commission are examining the billing practices



UNFAZED: Case expects growth to revive

of AOL and other online service providers. A government source cautions that the probe isn't a formal investigation. Regulators are concerned that online operators may not have followed FTC rules about unfair billing practices. The New York State Attorney General is also said to be looking at online services. "Several state attorneys general have informally inquired into industry practices," says an AOL spokeswoman.

TALLIES FOLLY. As the No.1 service, AOL may get the most attention. The company already faces 12 lawsuits from subscribers accusing it of overbilling. Among other issues, the FTC is examining whether online companies have made it hard to cancel service after a free trial. The spokeswoman says AOL is negotiating a single settlement for the suits and is discussing "routine" industry practices with the FTC.

Much of the criticism stems from how charges are tallied. AOL's \$9.95 monthly fee includes five hours of service; additional use is \$2.95 per hour. But instead of adding up the total time a customer spends online each month as Prodigy Services does, AOL and CompuServe Inc. round up each session to the next minute. AOL also adds 15 sec-

onds to each session for connecting and disconnecting. CompuServe and Prodigy don't.

In one suit, Stephen M. Case, a Palo Alto attorney, contends that AOL did not fully disclose its calculated bills. The suit alleges that AOL bills time spent in areas where users were supposed to be downloading and didn't refund money for canceled subscriptions. AOL says it has clarified its policies and refunded charges

incorrectly assessed for use of free

The flap comes at a bad time for the quarter ending Mar. 31, AOL's subscriber base grew only 19.8% to 10.5 million, compared with a 46% gain in the 1995's first quarter. Cowen & Co. analysts say growth could slow to 7.3% this quarter. Analysts such as David B. Reed at Montgomery Securities fear that the slowdown—at AOL and rivals—due to inroads by Internet service

Stephen M. Case, AOL's chief executive, says the reason is that AOL is back on marketing this spring. The promotion will resume when new software ships this fall. AOL is "uniquely positioned to bring interactive services to a mainstream audience," Case, and it still aims to hit 10 million subscribers in 18 months.

But what will they pay? AOL acknowledges that the Internet is putting

pressure on prices. AOL says it is seeking new sources of revenue, including online advertising. "they haven't figured out where the new revenues will come from," says Mark Mooradian, an analyst with Communications. Subscribers would prefer that it doesn't result from overbilling.

By Amy Bell with Catherine in Washington

TROUBLE ON THE LINE

BILLING PROBE Regulators are eyeing billing practices in online services

SLOWING GROWTH AOL's subscriber base grew 19.8% in the first quarter, down from 46% in 1995

INTERNET MANIA Internet services could force AOL to cut fees

The China Business Congress



China must now subject itself to the laws of a market economy."

Jiang Zemin, President, People's Republic of China, during a site exchange delegates of China Business Congress



is important for a foreign investor China to keep their eyes on the future, and to always maintain a spirit of cooperation. With these, you will find success in China."

Jiang Zemin, President, People's Republic of China

While Western Europe and North America wrestle with slow growth, China tops world expectations by enormous percentages, year after year. "Our target was to quadruple our 1980 GNP by 2000, said Sun Shangqing, President (Minister) of the Development Research Center of the ruling P.R.C. State Council. "We have met this goal five years ahead of schedule."

Enterprises of 160 nationalities are investing billions in the new, improved China. But even as they reap enormous benefits, foreign investors call for faster reform, better laws, and less regulation.

That is why the Development Research Center, the economic policy advisor to China's governing State Council, joined with *Business Week* and The McGraw-Hill Companies to create THE CHINA BUSINESS CONGRESS: a gathering designed for

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IN PARTNERSHIP WITH

THE DEVELOPMENT RESEARCH CENTER OF THE STATE COUNCIL OF THE PEOPLE'S REPUBLIC OF CHINA

AND

THE MCGRAW-HILL COMPANIES

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- AMERICAN INTERNATIONAL GROUP, INC.
- BANK OF AMERICA
- THE BOEING COMPANY
- HEWLETT-PACKARD COMPANY
- J.D. EDWARDS WORLD SOLUTIONS COMPANY

AND WITH THE SUPPORT OF WU ASSOCIATES

the sharing of perspectives between policymakers and the foreign investors whose capital and technology are so important to China's continued progress. Foreign investors responded enthusiastically, as did Chinese leaders. The number of ministers, vice-ministers, and industry directors attending and interacting with foreign investors overwhelmed all expectations.

Communists?

China is the fastest growing national economy on Earth. The casual visitor would hardly guess that this country was substantially different from other engines of economic growth.

But it is. Large state-owned enterprises retain a central role and the Communist government does not intend to privatize them. Ever. Foreigners participate principally through joint ventures and other cooperative arrangements with the government-run firms, enabling each state-run company to harness itself to the expertise, technology, financial wherewithal, and global market access of its foreign partners.

"We are moving from a closed state to an open economy," says Ge Hongsheng, Minister of China's State Council Office for Special Economic Zones. "Our links with the world economy tighten daily."

China continues to operate on a socialist command model, but unlike the old Soviet model, this one works. "The Fifth Plenary Session of the Fourteenth Communist Party Central Committee requires us to vigorously promote fundamental



"It is not wise for the U.S. to announce every six months what penalties we are going to inflict if China does not meet a certain set of conditions."

Dr. Henry Kissinger

chairman, Kissinger Associates; U.S. Secretary of State, 1973-1977; U.S. National Security Advisor, 1969-1975

by Scott Shuster, consultant to Business Week Executive Programs, and chair of The China Business Congress

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"Our target was to quadruple our 1980 gross national product by the year 2000. We have met this goal five years ahead of schedule."

Sun Shangqing*, President (Minister) of the Development Research Center of the State Council of the P.R.C., and a member of the Financial and Economic Committee of the National People's Congress

*Minister Sun, a leading figure in China's historic shift toward market socialism, passed away suddenly one week after the conference. The concepts and

enunciated at this international gathering continue to inform current policy setting in China.

AVIATION

"Aviation relates to virtually every business activity in China, while providing critically needed infrastructure," says **Kenneth E. Gazzola**, executive vice-president/publisher, Aviation Week Group. "It's no surprise that aviation is a central focus of Chinese government attention and investment." Mr. Gazzola and Michael Mecham, Aviation Week's Asian bureau chief, moderated a panel discussion on aviation.

SKY-HIGH SECTOR GROWTH

"In 25 years China has taken delivery of more than 250 Boeing airplanes," says **Ronald B. Woodard**, president of the Boeing Commercial Airplane Group. "During that same period our competitors have delivered another 70 or so. Now China wants another 240 airplanes in just five years. That's a big, big challenge."

And it's not only airplanes. China plans to build 11 new airports and undertake 30 large-scale airport renovations, by 2000, a colossal building program worth billions.

"The development of an aviation industry is the measure of a country," says **Zhu Yuli**, President of Aviation Industry of China, the umbrella group guiding one of China's fastest growing and most successful industry sectors. "High technology develops very fast in a modern aviation industry, and that is a central goal for us. However investment is large, the risk is very high, so we will offer expanded opportunities for foreign partners as we move to become a leading supplier of aircraft parts to the large international airplane companies."

shifts responding to new historical conditions." Minister Sun intones, with due solemnity. "So we will speed up reform of the financial, investment, and insurance systems!" "The National People's Congress adopted the Ninth Five Year Plan," avers Minister Ge. "This means we must extend our opening up and engage in more economic and technical exchanges, actively introducing foreign capital and intelligence and skills!"

What does it all mean? That China — by order of the Communist Party leadership — is directed to become more and more like everywhere else.

Joint Adventure

"Finding the right joint venture partner is absolutely critical to success," says **Vincent H.C. Cheng**, OBE, JP, former Hong Kong affairs advisor to the P.R.C., and member of the Hong Kong Executive Council. "Strong Chinese partners can insulate the business from official impasses. Relationships must be cultivated at the grassroots as well as the top levels. Encourage official input. Negotiate, never confront."

"We formed our joint venture in 1985. Discussions had begun in 1982," **Lee S. Ting**, vice-president and managing director, Asia Pacific of Hewlett-Packard Asia Pacific Ltd., recalled the days when China's opening was new. "Things were very fuzzy. There was no Chinese legal system to guide us. But in an environment where you expect change, you cannot wait for things to settle. That day may not arrive for a long time. And if you wait until then you will be too late."

"We have invested... \$100 million in China's aviation infrastructure. It's a good investment."

Ronald B. Woodard, president, Boeing Commercial Airplane Group



More recent arrivals in certain businesses are finding China ready to let them operate on their own, with no local partner. "Our experience here has been accelerated," says **Mike Sheppard**, vice-president and managing director Asia Pacific for J.D. Edwards World Solutions Company, a U.S. software developer for the manufacturing, distribution, construction, and energy-chemicals industries. "Three months after arriving we received our wholly foreign-owned enterprise license and we began hiring. The key for us, a servative, privately-held company was our ability to meet the authorities. I brought my tax director to the authority meeting. The authorities are very cooperative. Our experience has been above all very positive."



"You cannot wait for things to settle and become clear. That day may not arrive for a long time."

Lee S. Ting, vice-president and managing director, Asia-Pacific, Hewlett-Packard Asia Pacific Ltd.

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Action Plan

THE CHINA BUSINESS CONGRESS was a big for trouble. The Chinese leadership was looking for solutions to the problems confronting their foreign partners. Foreign executives were eager to contribute to development of an "action plan" to improve the business environment. Neither side was disappointed. "The business environment," one Chinese official pointed out, "is created by all of us, together."

THE 'THREATS AGAINST CHINA' PROBLEM:

"There is a tendency to use trade for political pressure," said one Chinese official. "Is it for one country to use trade as a method of trying to change the structure of a friendly government? This is not an appropriate instrument and it has consistently failed. Trade should not be used as a nail."

THE CHINA-U.S. RELATIONS PROBLEM:

We need regular dialogue at the very highest level between the two systems. There has not been a genuine exchange of presidential visits between our two countries since the 1980s. We need a solid bilateral relationship, with a shared vision based on shared interests — the interests of common prosperity and peace. We can be strong together."

THE COST OF DOING BUSINESS:

"There has been a rapid increase occurring in the cost of labor. It is coming close to the cost elsewhere in Asia. It is far too quick and is causing concern to foreign investors."

REGULATIONS AND RULE CHANGES:

"Red tape is stifling. New fees, new policies, new hurdles. One day, profits are limited to 12%, the next day, it's 15%. Lenders and banks are saying 'gentlemen, when the rules are clear, we'd like to invest.'"

UNEVEN PLAYING FIELD:

"We occasionally still see non-competitive ministry-directed enterprises chosen for certain activities, who expect to get an unusually high price for their work. We don't like that."

FINANCIAL SECTOR REFORM:

"There comes a point when integration with the rest of the world dictates that you bring your financial sector up to speed. At that point, if you don't act you can run into serious problems—as Mexico did."

THE SYSTEM BOGS DOWN:

"The plans are in place, the orders are promised publicly, but then the system bogs down. Everybody's in charge and we don't get the promised orders processed by the central government."

China's business challenges are now mostly predictable, so correct project design can avoid many problems," says **Dr. Michael Wu**, principal of China turnaround and strategy consultants Wu Associates, of Ridgefield, Conn. "Remember that China remains a planned economy. What you do must fit into the plan. Make certain that the activities you undertake resonate with the government's development goals. Do not try to replicate strategies that worked in other countries. China needs a unique strategy, both for entry and for sustained success."

The China Business Congress



"It has been exhilarating. The key for us was our ability to meet the authorities."

Mike Sheppard
vice-president and
managing director
Asia-Pacific,
J.D. Edwards World
Solutions Company



"We are moving from a closed state to an open economy. Our links with the world economy tighten daily."

Ge Hongsheng
Minister,
State Council Office
for Special Economic
Zones, People's
Republic of China

CONSTRUCTION

"With more Chinese moving to the cities, housing needs are expected to top 25 billion dollars," enthused **Eric** [unclear], senior vice-president, Construction Information Group, The McGraw-Hill Companies. "Meanwhile, the industry of Electricity has targeted an incredible 15,000 megawatts of annual development. Power plants, housing, highways, water treatment, buildings of every description — everything is needed on a grand scale. Investment in Shanghai alone could top \$100-billion."

Enthusiasm warranted. But **Yao Bing**, Director, Department of Construction Industry of China's Ministry of Construction is under no illusions. "We have serious tasks to fulfill, but we lack funds," says Yao. "We welcome foreign financial institutions and contractor colleagues from abroad."

BUILDING A NEW SYSTEM

"There has been tremendous progress here," says contractor **Richard Erskine**, vice-president and manager of Bechtel China, Inc. "They have moved from a state-controlled system of design and construction to a free market system in just five years. They've lowered their costs. They're getting projects built quicker."

"Construction manufacturing has seen remarkable change. We are now buying Chinese materials: very good quality at very good prices. And among Chinese contractors we are now seeing consistent schedule compliance, consistent improvement in quality in all ranges of major projects, delivering great assets to the owner. It has been a remarkable improvement."

"This is really a good time to invest in China."

The China Business Congress



"The authorities and we on the foreign side can work together to improve the environment for future investment."

C.M. Pang

senior vice-president and
country manager-P.R.C.
Bank of America



"If we can get more of our legislators to visit China we will have a more mature and reasoned approach on their part."

James R. Sasser

U.S. Ambassador to
The People's Republic
of China

BUILDING A FINANCIAL SECTOR

"The Chinese securities market is not mature, and neither are the shareholders. That is why you see abnormal phenomena on our exchanges." These words from a senior figure of the China International Trust and Investment Company (CITIC) exemplify the new, open spirit of China's financial leaders.

"Some of our regulations are not well implemented," the official continues, "Our market management mechanism is not perfect. There are still some speculative activities. Performance of our listed companies has been so satisfactory. But listen to the direct investors. Many have been very successful because they did not come to 'hit-and-run.' It should be the same for institutional investment. If you want to be here for our bright future you need patience and persistence."

"China's 1995 inflow of foreign investment was second only to the U.S.," says **C.M. (Chung Min) Pang**, senior vice-president and country manager-P.R.C. Bank of America, "You can get all the capital you want for equity investment in China."

"But," Pang explains, "it is almost impossible for a corporation to get debt financing. Banks fall over backward to lend to state financial institutions because the monetary authorities are managing debt very tightly. This wins them very fine pricing."

"Outside the guaranteed environment, however, regulations are not very clear, the legal system is particularly unreliable, and therefore risk is perceived to be excessively high. Very high rates are charged. This forces China to give away benefits they would not have to give away in a more transparent market."

"This is an area where the authorities and we on the foreign side can work together to improve the environment for future investment."

Political Threats

International politics repeatedly emerged as a complicating factor in business relations, particularly between the U.S. and China.

"Difficulties in our bilateral relationship may start impinging on some of our trade relations. I think that's very regrettable," said **James R. Sasser**, U.S. Ambassador to China. "Our legislative branch exercises more influence over U.S. policy than is the case in most other democratic countries. I think if we can get more of our legislators to visit China we will have a more mature and reasoned approach on their part."

In a gathering at The Great Hall of the People, the same day as the visit of Zhou Enlai and Mao Zedong in the first phase of U.S.-China rapprochement in 1972, Dr. Henry Kissinger warned that "it is not wise for the U.S. to announce every six months what penalties we are going to inflict if China fails to meet a certain set of conditions developed in Washington. We have no fundamental conflicting interests. China will become a great power and have greater influence. We have to get used to this."

David M. Lampton, President of the National Committee on U.S.-China Relations pointed out that, "Business is the major constituency that understands what's at stake here in China, but business is not enough to carry the day in our pluralistic system."

"If most Americans had even the foggiest idea of the change that has occurred in China they would be cheering. It's not malevolence, it's ignorance. The first time in 1991 I took a number of

TEN YEARS OF SUCCESS FOR BUSINESS WEEK/CHINA



From the left: David G. Fern, publisher, *Business Week*; Sun Yonghai, former president, China Foreign Economic Relations and Trade Publishing House; John W. Patten, president emeritus, *Business Week*; Stephen Shepard, editor-in-chief, *Business Week*; Sun Hanchao, president, DRC

"People told me, 'It's too early, Jack!' But Hank Greenberg at AIG and Mel Stanford at Boeing advised me to go for it, and we created a Chinese language edition of *Business Week*. I'm proud that The McGraw-Hill Companies have been early participants in the new China."

John W. Patten

President Emeritus *Business Week*

"*Business Week/China* was the first periodical to be co-published by China and the United States. This successful collaboration with The McGraw-Hill Companies has helped us gain a better concept of the world, and plays an important role in improving China's international, industrial, and commercial cooperation."

Sun Hanchao

former President, China Economic Relations and Trade Publishing House

BusinessWeek

EXECUTIVE PROGRAM

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SCIENCE'S NEW NANO FRONTIER

quest: To build supercomputers molecule by molecule

Anyone who is not shocked by quantum theory has not understood it," said Niels Bohr, one of the 20th century's premier physicists. In the quantum world—the

land of atoms, electrons, and other very things—cherished notions of reality collapse. Bits of matter can be in more than one place at the same time. Electrons tunnel through impenetrable barriers. And some say quantum theory allows the possibility of multiple universes.

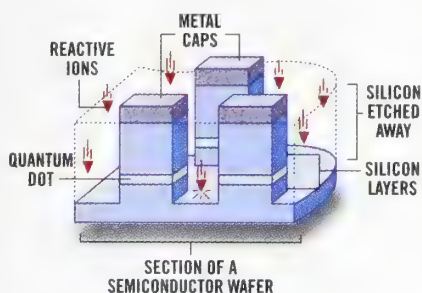
One of this strange quantum behavior, which mattered only to theoretical physicists, has major implications for the electronics industry. Quantum conductors have taken to the point of the behavior of individual atoms and electrons will soon begin to matter. Quantum effects are starting to take over, changing all the rules. As chipmakers learn to harness quantum mechanics, growth in computer power and everything else that depends on chips will come to an end.

TIME. Around 2010, the width of lines etched on semiconductor wafers will be narrowing to less than one-tenth of a micron. Electrical signals passing through those lines will have so few electrons that adding or subtracting a single one will make a difference—putting chipmakers squarely in the quan-

tum world. "At that point, we better have a new technology ready to go into production," says Gary A. Frazier, manager of nanoelectronics at Texas Instruments Inc.

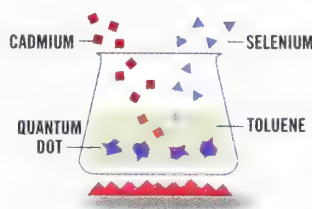
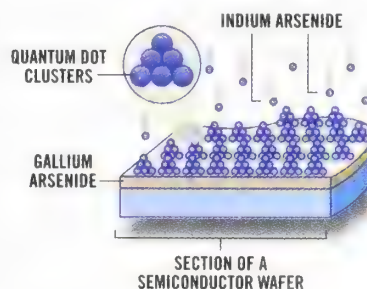
HARNESSING QUANTUM DOTS

Quantum dots are the smallest electronic structures scientists can imagine. In the 21st century, they may lead to vastly smaller, yet far more powerful, chips and lasers. Here's how researchers are making quantum dots today:



ETCHING PILLARS Print metal squares on the surface of a semiconductor wafer that has an ultrathin quantum layer of gallium arsenide sandwiched between two layers of silicon. Etch away the silicon, using ions that won't erode the metal squares, to expose the quantum layer.

GROWING CLUSTERS Coat a semiconductor wafer with gallium arsenide. Shower the wafer with molecules of another semiconductor, such as indium arsenide. The falling molecules bind to the gallium arsenide—and act as seeds. As more molecules rain down, they attach to the seed molecules, forming cannonball piles.



PRECIPITATING CRYSTALS In a solvent such as toluene, dissolve the ingredients for a two-part semiconductor—say, cadmium and selenium. Add a reagent to prevent the solvent from contaminating quantum dots. Heat carefully so that only a few atoms combine. Result: crystals small enough to be quantum dots.

That's why scientists around the world are rushing to probe what University of Wisconsin materials scientist Max G. Lagally calls "the last great frontier in solid-state physics." Lagally and others have made tiny structures called quantum dots that can hold single electrons. They are so small that billions could dance on the head of a pin. Researchers have used quantum dots to fashion transistors that switch on or off with movements of a single electron. And they've concocted clever arrangements of quantum dots that could serve as the guts of tiny, powerful computers. "It's a fun time," says Yale University electrical engineer Mark A. Reed. "The field is exploding, and there's a lot of good going on."

The current research involves long-range, basic science. "We have to understand the new physics, new properties, and new devices that might be possible at these smaller scales," explains IBM chemist Christopher B. Murray. Indeed, the quantum devices being built or contemplated today may never prove economically feasible. But the notion of building tiny structures molecule by molecule, incorporating advances in chemistry, physics, and materials science, is "bound to have a tremendous payoff," says University of Notre Dame physicist James L. Merz. The promise has led companies such as Texas Instruments, IBM, Hewlett-Packard, and Motorola to back major research efforts.

The main goal of such research is to control the movement of very small groups of electrons without running afoul of weird quantum effects. Quantum dots could make that possible. These dots are clumps of matter less than 20 nanometers wide—that's 20 billionths of a meter, or about the length of a string of 60

silicon atoms. If such a clump is engineered from atoms with just the right properties, it can turn a free-spirited electron into a caged canary. The electron can't escape without a precisely sized boost of energy from the outside.

This "quantum confinement" gives rise to some interesting phenomena. It makes possible the small, highly efficient lasers already in use in many CD players. These so-called quantum-well lasers are made of an ultrathin layer of semiconductor material sandwiched between two layers of another material. Electrons in the middle are trapped in a quantum flatland, able to move in only two dimensions. That makes it easier to pump energy into them in the way needed to produce laser light. The result: more light produced from less power.

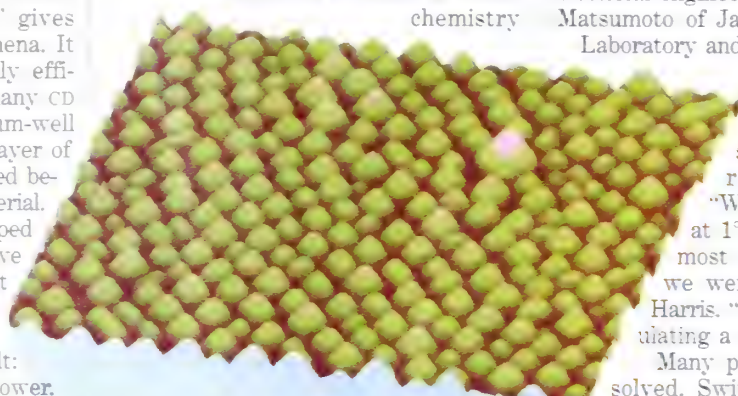
At Bell Laboratories, owned by AT&T spin-off Lucent Technologies Inc., researcher Loren Pfeiffer is delving even deeper into quantum research. He lops off one more dimension from the flatland and makes lasers based on so-called quantum wires. Inside, electrons can move in only one direction. Quantum-wire lasers can emit light at power levels beyond the practical limits of quantum-well lasers. "That could prove an overwhelming advantage for communications," Pfeiffer says. These higher-power lasers may reduce the need for the expensive repeaters installed every 50 miles or so on telecommunications lines to regenerate laser pulses, which degrade as they travel through optical fibers.

Scientists expect more gains by moving from quantum wires to quantum dots. But the quantum-dot lasers that researchers have built haven't lived up to expectations. For various reasons, including the difficulty of making these clusters exactly the same size, "the dots are not as useful as people thought they would be," says researcher Gilberto Medeiros-Ribeiro at Hewlett-Packard Co.

The first challenge is to find a way to mass-produce quantum dots of nearly identical size. Two leading methods are to etch pillars in semiconductors and to deposit clusters on top of them (diagram, page 101). Some researchers are spurning these techniques in favor of chemistry. For instance, Louis E. Brus, a physical chemist at Bell Labs, has pioneered a method that grows quantum-dot crystals in a test tube, molecule by

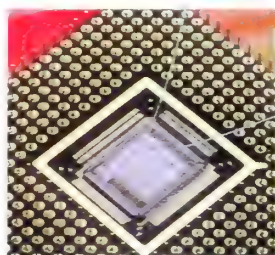
molecule. Using this technique, researchers have built light-emitting diodes that can be tuned to different colors.

Even more exotic are the quantum structures made from single organic molecules in James M. Tour's chemistry



lab at the University of South Carolina. This approach offers the tantalizing prospect of packing trillions of molecule-size devices onto a square millimeter. That single millimeter would contain 10,000 times more transistors than now found in a PC.

The ability of quantum dots to grab and hold electrons is essential if computing functions are to be performed



NOW THAT'S PORTABLE

Single-electron transistors have already been crafted that, in theory, make it possible to store 15,000 times more data on a chip than those produced today

by movements of single electrons. Physicist Konstantin K. Likharev of the State University of New York at Stony Brook has constructed a model memory chip with quantum storage dots. Single-electron transistors "read" the contents of the dots by sensing the electrical field of a trapped electron. On paper, his design could store a terabit of data—that's a trillion bits, or 15,000 times more than existing chips can store—on a chip about the same size as those used today.

A number of research teams have crafted the single-electron transistors needed by Likharev's model. In 1993, for example, a Hitachi-funded lab at Britain's Cambridge University announced it had constructed an experimental single-electron memory device. Last July, it unveiled a single-electron logic structure.

Most quantum devices work at extremely low temperatures. Even the

slightest heat makes electrons too bunctious and swamps the tiny quantum effects. However, by carefully engineering materials to give quantum tighter grip on their electrons, electrical engineers, including Kazuo Matsumoto of Japan's Electrotechnical

Laboratory and Stanford University

James S. Harris

have recently

single-electron

sistors that work

room temperature

"When we were working

at 1° Kelvin [minus 459° Fahrenheit]

most of the world thought

we were really crazy,"

Harris. "Now, the work is

stimulating a lot of research."

Many problems remain

solved. Switching speeds can

slow, and a single electron is easily

diverted from its intended path by a

electrical energy. So instead of trying

design quantum imitations of today's

computers, most scientists are hard at

concocting radically new approaches

SQUARE DANCE. At the University

Notre Dame, Craig S. Lent and his

theorist Wolfgang Porod have come

with a scheme in which the basic

building block is a square containing

quantum dots. When two electrons

are added, they back into opposite

corners. So the square has two possible

configurations: electrons in the top left

and bottom right corners, or in the top

and bottom left. This is just what's

needed for a switch—and it can be

flipped back and forth by the

movements of electrons in neighboring

squares. That means these squares

can be arranged to duplicate all the

functions needed for computing. So

Lent's team has managed only to

test pairs of dots to test the physics

of the initial results are "stunning,"

Lent. "I was prepared for them to

work as well as they do."

Whatever technique proves to be

the best way of building quantum

computers, it's years of painstaking engineering

ahead. "Quantum computing is

out there, right now, it's just some

fun to scratch our heads about," says

Stanley Williams, head of Hewlett-Packard's new quantum effects lab.

Researchers foresee a day when

trillions of quantum dots could be

stacked on top of each other, layer

by layer, on otherwise conventional

silicon. That promises a supercomputer

on a pinhead—making these

structures part of the hottest boom

on the quantum frontier.

By John Carey in Washington

Heidi Dawley in London

EDITED BY OTIS PORT

BUILDING BETTER E-BIKE DESIGNS

A BICYCLE IS THE PRIMARY means of transportation for more than half the world's people. It doesn't pollute, and riding it provides good exercise. Yet most engineers don't give it a second look. Owens Corning of Toledo, Ohio, aims to change that with its Global Design Challenge. It asked for top design and engineering schools in the U.S., Canada, Germany, France, China, Hong Kong, and Brazil to design a bike that would cost less than \$100 and use glass-fiber composites as primary material. The winners: Seven



designs from the University of São Paulo in Brazil. Their Kangaroo design boasts an adjustable wheelbase: short for maneuvering in traffic, long for leisure riding. The seat and handlebars can be raised or lowered to fit 95% of the globe's population, the team says. The frame, they chose Kevlar reinforced with carbon fiber and glass fibers. And the estimated manufacturing costs for a bare-bones model to be about \$100. Owens Corning is now soliciting offers from manufacturers. *Peter Coy*

DEATH RAYS TO ZAP DIESEL POLLUTION?

WHEN MARTIN GUNDERSEN AND VICTOR PUCHKAREV MET IN 1993 at a scientific conference in Russia, they clicked instantly—even though they had been at each other's throats during the cold war, working on ways to shoot down the other side's missiles. So Gundersen, an electrical engineering professor at the University of Southern California, invited Puchkarev to join him at USC and help turn their weapons knowhow into a pollution zapper.

Today, they're downsizing the pulsed-power beams that Gundersen helped develop for the Pentagon's Star Wars program. The goal is to clean up diesel-engine exhausts by rapidly shooting high-voltage power pulses through the tailpipe. The pulses unleash an electrical plasma of hordes of fast-moving electrons. In turn, the electrons trigger an avalanche of chemical reactions that break down nitrogen oxides, a key cause of smog, into pure nitrogen and pure oxygen.

Gundersen is working under a contract with the U.S. Navy, which has orders to reduce emissions from its diesel-powered ships. Diesel engines are more fuel-efficient than conventional engines but produce more nitrogen oxides. Various companies have attempted to deal with that using exotic fuels and special catalytic converters. But Gundersen says an electric plasma system should be cheaper and could be used with existing engines, not just new ones.

Gundersen and Puchkarev have outfitted an old diesel-powered Volkswagen Golf with a prototype, but it's not practical. The device is too big and needs too much energy to generate the power pulses. Part of the solution may lie in faster, shorter pulses—each lasting just five billionths of a second. While that's beyond the scope of existing technology, Gundersen expects to get there, and shrink the unit's size, by 1998. □



A PHOSPHATE-FREE DIET FOR BACTERIA

THE U.S. SPENDS MORE than \$5 billion a year to get organic matter such as dead leaves out of water supplies. Conventional wisdom says that because

bacteria feed on organic matter, getting rid of the stuff will reduce the amount of bacteria in drinking water.

But water experts may be barking up the wrong tree, according to scientific correspondence in the June 20 issue of the journal *Nature*. It turns out that bacterial counts can be reduced more efficiently by depriving the microbes of phosphates, say the letter's authors, Ilkka T. Miettinen, Terttu Vartiainen, and Pertti J. Martikainen of the National Public Health Institute in Kuopio, Finland.

The researchers fingered phosphates as the critical nutrient after noticing that, contrary to expectations, microbial growth was lower in water with more organic matter.

Peter Coy

INNOVATIONS

■ The technology that inflates air bags in cars may soon be helping to snuff out fires. The National Institute of Standards & Technology is working with the Navy and Air Force to test solid-propellant gas generators—automobile air-bag inflators without the bag. The aim is to use them to suppress fires in ships and planes by spewing out gases that displace the oxygen needed for com-

bustion. The concept might also work in factories and warehouses.

■ Rechargeable lithium batteries pack twice the power of other rechargeables, but they contain toxic materials, particularly cobalt compounds in the negative electrode. So researchers at the University of St. Andrews in Scotland have developed a negative electrode that uses manganese instead. Manganese costs less than 1% as much as cobalt, is far

less toxic, and performs about as well.

■ The sweet smell of pig manure? That's right—thanks to peanut shells, says Evan E. Jones, a professor of animal science at North Carolina State University. Jones says that mixing half a ton of shells with a ton of manure eliminates malodors within two days—and within two months the mixture turns into a nutrient-rich compost that looks and smells like soil.



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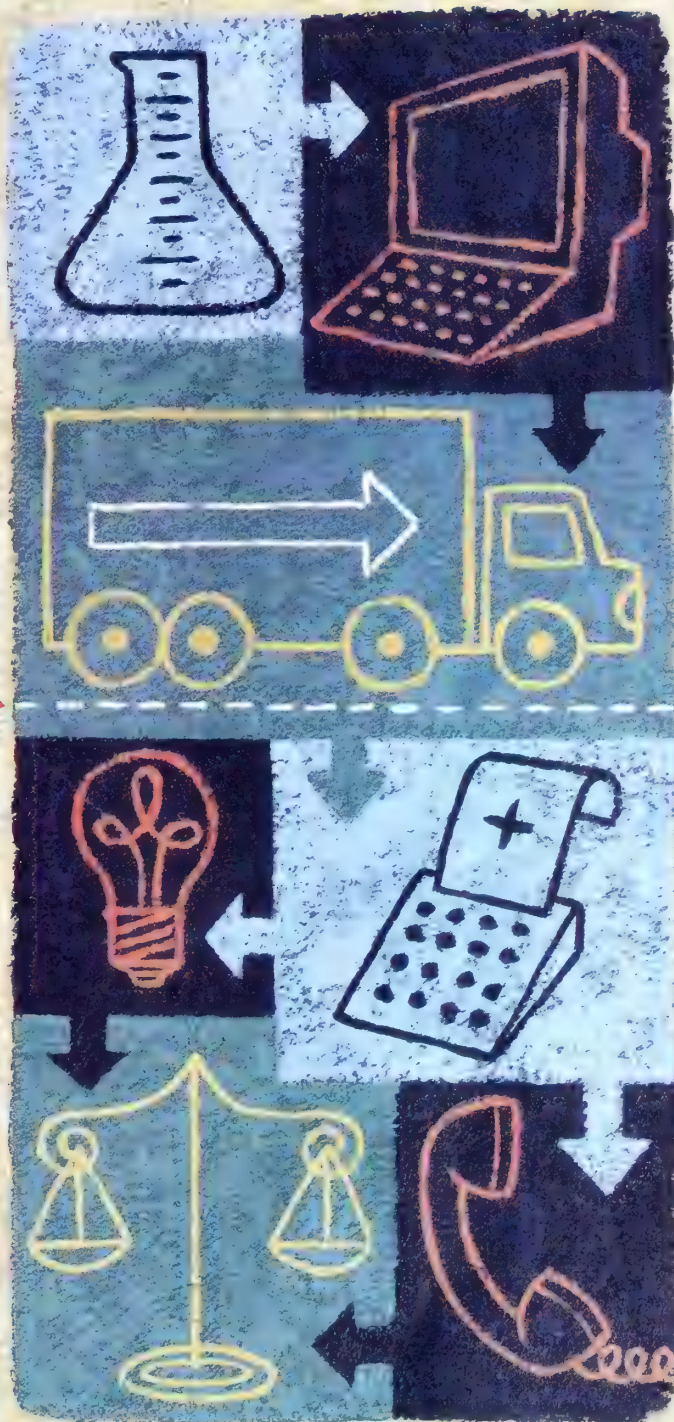
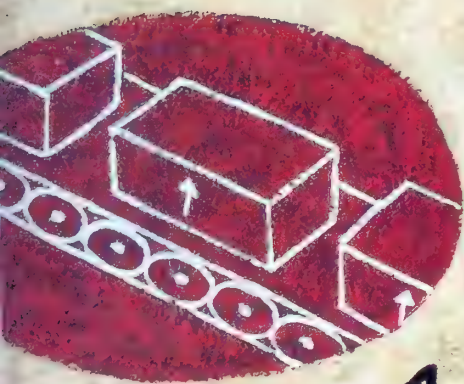
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Solution Sourcing

The Make vs. Buy Decision for Corporate Services



solution sourcing



Sourcing Strategies

Today's businesses are refocusing their efforts on their core competencies and getting back to what they do best.

While product "make vs. buy" decisions have long been on

management's agenda, effective sourcing strategies for corporate staff services has become a critical issue in the search for increased effectiveness, profitability, and corporate performance. Third-party service providers increasingly bring advantages of scale, skill, cost, and efficiency over in-house solutions, and savvy business leaders are seeking sound advice for the right mix of various sourcing alternatives to services traditionally performed in-house.

Growing revenue and profits is a more rewarding challenge than saving our way to prosperity by driving out inefficiencies

or improving the effectiveness of corporate services. Fixing what really needs to be done well, in conjunction with achieving core competency objectives and implementing selective sourcing strategies will better enable businesses to achieve their respective value propositions.

Solution sourcing is a logical approach towards corporate service delivery. Done smartly, it can result in shared sourcing arrangements with other companies or between independent units of a larger organization. Sometimes, it requires insourcing externally provided services.



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More often, however, solution sourcing demands new supply chain partnerships with key customers or suppliers where interests strongly overlap. It usually requires the selective outsourcing of essential, but not strategic, services. The list of such services continues to grow, and includes accounting, customer service, facilities management, finance, human resources and staffing, information technology (IT), logistics, printing, and telecommunications. Even functions such as document management have become candidates. "As organizations increasingly think about and work with their documents as assets," says Paul A. Allaire, Xerox chairman and CEO, "outsourcing has become one of the fastest-growing segments of our business."

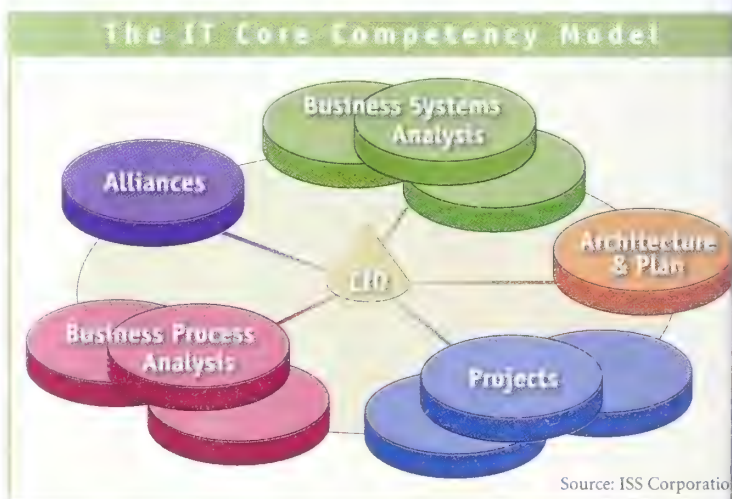
Solution sourcing can become the means to arrive at the competency requirements to grow and sustain businesses as they adapt to an ever-changing marketplace. Sourcing's principle objective is the alignment of the delivery of corporate services with the business. To succeed, it demands a holistic evaluation of core competency requirements, business architecture, and organizational change within the context of business strategy and growth objectives. Too often, outsourcing is seen as a piece-part that results in one-off behaviors that serve to defocus management attention from the real mission. "Collaboration is key," says Ami Kaplan, partner at Deloitte & Touche. "Cosourcing between clients' organizations and their sourcing partners is a welcome approach to

more confrontational forms of outsourcing."

The Solution Sourcing Value Proposition

Arriving at the correct value proposition requires an assessment of the relative strategic importance of corporate services. While the cost element has historically dominated

tions of core competencies and sourcing decisions are possible. One company, for example, selectively outsourced virtually all of their IT transaction systems. Certain IT skills, however, were part of a defined core competency, and were exported directly into the business organization. The IT professionals were allowed the flexibility to work



the drive to outsource, increasingly the driver is for businesses to reduce the need to directly provide non-strategic services in order to focus resources on what they must do really well. To achieve this, businesses must fully understand their core competencies and incorporate that knowledge into a value proposition analysis.

Core competencies are the skills and knowledge that are fundamental to the business, and they are relatively few in number. They are probably already known to key customers; are leverage points in the value chain; and should be the basis of the business' distinctive competence. With a balanced analysis, unique and powerful combina-

independently within the business, and, operating largely through influence, find and translate business opportunities into IT solutions that in turn were delivered through selectively sourced systems development.

Another organization came to the conclusion that supply chain and "back office" services (e.g., accounting, finance, human resources, and legal) across a loosely held group of businesses were clearly not strategic. They consolidated these back office services across the corporation to form a shared services organization with essentially the same terms and value proposition as would have occurred with outsourcing. They outsourced actual manufacturing and distributive



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to an organization that specialized in their type of product and distribution channels. The end result was focused selling organizations with shared corporate services and outsourced supply chain processes.

Conducting the Sourcing Value Analysis

A technique we believe gets at the real value proposition breaks out the business' key corporate services into high level processes and then subjects each to a forced ranking in terms of their strategic importance and core competency to that business. When conducted in a rapid results workshop with senior business management, this technique provides the first clue to possible candidate processes for solution sourcing.

A manufacturing company firmly believed that the customer service process was the most strategic of its corporate services. After significant reengineering expense and the building of essential core competencies, however, performance was still inadequate. Working with the close support of key customers, a joint decision was made to export the company's customer service agents into key customer production planning processes. The result was a virtual organization between the company and their key customers.

Non-strategic services that are outsourced should not automatically remain that way. If the quality performance of the process is outstanding, and it can be effectively insourced, it may provide an opportunity for revenue generation. A financial ser-

vices company outsourced the development and support of an electronic mail distribution system that had such good quality and cost performance that the client decided to bring it back in-house and extend it as a service to other companies, including the competition.



Sourcing analysis can produce a variety of results

Opportunity Identification

A balanced sourcing analysis can produce a variety of results. New product development in a fashion goods manufacturing company is a case in point. The ability to produce creative new fashions that customers will buy is the soul of the business – the “secret sauce” will never be shared with external parties – and that ability will be maintained in-house. A concept in creation, however, needs to be turned into graphical design representations. For some companies, this activity is best supported by selecting a specialist design firm to provide

quick response, rather than building or sustaining an internal capability. This amounts to selecting their core competency to support the manufacturer's strategic process. They are more likely to be able to staff, train, and support these scarce and expensive skill sets better than the manufacturer.

Actual development of the new product, including chemical analysis and product fabrication, is also a core competency for this company. The long-term industrial knowledge derived from manufacturing needs to be preserved and protected. Instead of outsourcing, the manufacturer turned to a sister company with advanced laboratory capabilities, and exported the service to them under the strictest secrecy. Similarly, the knowledge

and skill required to measure customer appeal – strategic

though this is – could best be achieved for this manufacturer through outsourcing to a marketing testing organization. Distribution and warehousing of new products was outsourced to a third party packer and distributor with core competence in supply chain logistics. This combination of approaches dramatically improved time to market even with additional parties involved in a highly proprietary process. In this example, a clearly identified strategic process will be supported by a handful of core competencies that depend upon a variety of smartly sourced activities.

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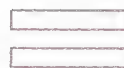
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Achieving Core Competency Requirements

Even in a strategic process, every skill set and knowledge base is not a core competency. Conversely, in a non-strategic process, not every skill set and knowledge base is automatically not a core competency. Finally, not every core competency needs to remain insourced. The criteria for achieving core competency status in one IT organization rested upon the contention that, while all skills are essential, some may be strategic or proprietary to the business. Skills to conduct transactional, structured, and largely repeatable processes are not likely to be considered core competencies.

Powerful skill sets that enable one-time events (such as systems development), or that are generic or highly portable, are often better bought in the open market than staffed as a core

competency. Conversely, skill sets that are tightly integrated (such as business systems analysis), or that support highly relational work processes with emphasis upon unique business knowledge are more likely to be deemed core competencies. To succeed, businesses will have to look beyond their own skills. "In the 21st century, it will be necessary to supplement one's own core competency – in our case, mobility – through

alliances to provide customers with a total positive experience," says Tom Scott, vice-president and general manager of Toshiba America, Inc.

Achieving Organizational Readiness

Whether or not the core competencies can be readily staffed and organized is another matter for many organizations. Honestly and rigorously assessing organizational readiness for the sourcing process is part of a risk management analysis. Organizational readiness can very well inhibit or delay implementation of the sourcing strategy. To bridge the gap, it is often necessary to strategically source to a consulting firm, an outsourcing vendor, or some other respected change agent.

In the case of the IT organization described above, there were five core competencies iden-

tified for insourcing. These included the chief informa-

tion officer (CIO) who operated as a peer with senior business management. A core team of senior individuals comprised the remaining core competencies. Sharing a reporting responsibility to the CIO and business leaders were a handful of senior business analysts – recruited from the businesses – to find and translate business opportunities into systems solutions. Another small handful of process-specific systems analysts spanned the

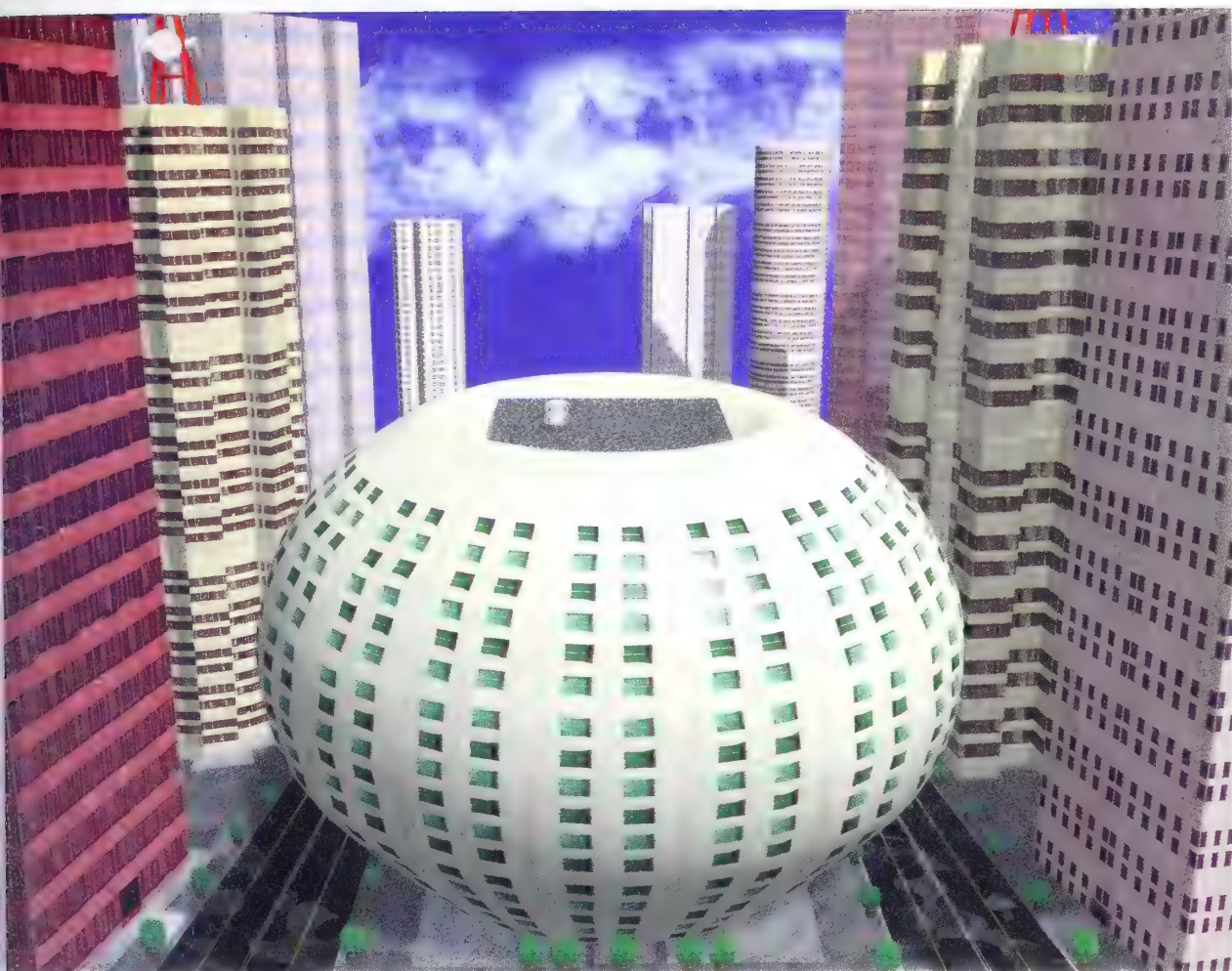
business segments and supported process improvement for the top three strategic processes. Another individual managed the IT plan and related architecture. Completing the core team was an alliance manager who conducted the sourcing analyses and managed all outsourcing relationships. A core team total of less than 10 individuals supported all information technology processes for a multi-billion dollar manufacturer. This is one highly successful implementation of what we call the core competency model.

Managing the Sourcing Process

Given the desire to proceed with external sourcing relationships, there is a need for solid internal management processes to manage those relationships. This will help manage the boundaries and accountabilities. Baselining current performance levels around specific metrics will provide a basis of comparison to later determine if the business is really deriving the intended benefits. One of the frequently outsourced IT processes, the Help Desk, is a good example. Nor can processes such as these be viewed in isolation. "Providers of end user support services must have end to end technical knowledge, and understand the relevant business context," observes Ralph Kelsey, vice president of customer support for GE Information Services. The partner selection process is the most important of all solution sourcing activities – but not from the usual perspective of function/performance/cost. Te



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real value is to smartly select the right kind of agent for the task at hand. Outsourcers generally fall into one of four classifications, depending on how they got their start.

Strategic partners are truly a rare bird. They assume the role of permanent trusted advisors, and assist in the development and implementation of strategy. Clients can gain access to knowledge, methods, processes, and technology not otherwise available. They are usually expensive, not apt to be amenable to fixed fee arrangements, and operate through small, highly leveraged teams of seasoned professionals.

Selective outsource partners are the classical outsourcers that provide support for repetitive, transactional-in-nature services such as distribution or data center management. Key selection criteria are domain expertise plus performance and cost. Fixed fee arrangements are the norm. Trust-based arrangements are unlikely, as service level management and performance penalties should operate to establish a desirable separation of responsibilities.

Specialist outsource partners are providers of highly specialized skills and capabilities or major one-time project management. Trust-based relationships are possible in the former, given the high probability of repeat business. Trust-based relationships are unlikely in the latter, given the demands and issues associated with large-scale projects. Key

selection criteria in both cases are domain expertise and performance. In IT, PC procurement and maintenance is a good example of specialized skills, and systems integrators are a good example of one-time major project management capabilities. Fixed fee arrangements are possible, but time and expense arrangements



Partner selection is most important

are more likely. Big Six and related consultancies dominate the large-scale project arena. Smaller boutiques tend to provide the best specialist skills.

Resource partners provide relief from one-time, or interim staffing shortfalls. They are an excellent hedge to minimize insourced skill build-up for one-time events, such as tax preparation. Key selection criteria are skills qualification, performance, and cost. Trust-based relationships are possible, given the high probability of repeat, or continuous business. Programming "body shops" are a good example. Fixed fee arrangements are

possible and they tend to be affordable.

Most potential partners stand in one of these domains. Almost all have attempted to "swim out" of their original competency, often with mixed results. Others have attempted to acquire other competencies through merger and acquisition with an equally mixed outcome.

Conclusion

Solution sourcing is about increasing organizational productivity through a balanced, common-sense approach to providing corporate services. The best way to achieve this is leadership by example, management by results, short-interval project management, and honest and open communications. The saviest companies realize that a

strategic sourcing strategy is required to ensure the best return on their sourcing investment. This requires an objective,

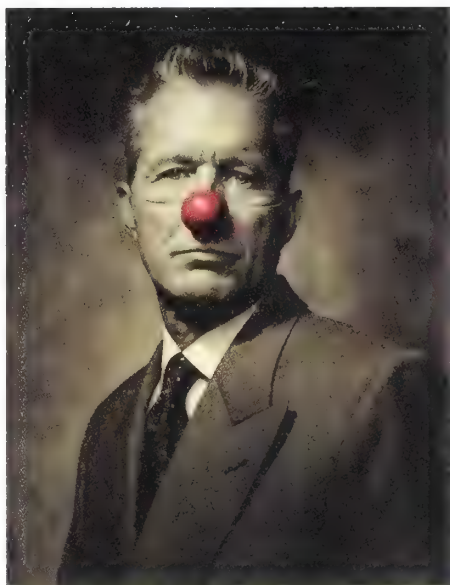
disciplined analysis and alignment with corporate core competencies to implement the correct sourcing "mix" for the long-term health of the business. Any well-managed company should demand no less.



Written by L. Hoy Heise and Robert L. Howie, Jr., vice-presidents of ISS Corporation, a consulting firm that helps operationalize strategy through a holistic approach to business, technology, and change. 1.800.DIAL.ISS or rhowie@800.dialiss.com.

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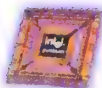
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1. ☐ Agriculture 2. ☐ Mining, Construction 3. ☐ Manufacturing, Processing 4. ☐ Wholesale, Retail Trade
5. ☐ Finance, Insurance, Real Estate 6. ☐ Government 7. ☐ Transportation, Public Utilities
8. ☐ Service Industries 9. ☐ Other - Please Specify:

What is your title?

- A. ☐ Chairman of the Board B. ☐ President C. ☐ Vice President D. ☐ Treasurer, Secretary E. ☐ General Manager
F. ☐ Division Manager G. ☐ Department Manager H. ☐ Other Manager I. ☐ Student J. ☐ Other - Please Specify:

How many employees in your company worldwide?

1. ☐ Under 100 2. ☐ 100-999 3. ☐ 1,000-2,499 4. ☐ 2,500-4,999 5. ☐ 5,000-9,999 6. ☐ 10,000 or more

EDITED BY AMY DUNKIN

UNLOCKING THE MYSTERIES OF TERM LIFE

At one time, if you wanted to buy life insurance coverage, insurance agents and the occasional savings bank were the only games in town. But now all kinds of financial-service companies are getting into the act, from discount brokers to direct marketers to commercial banks. The explosion of new sales channels gives consumers more choices than

ever. It also means they have to make an extra effort to ensure they understand the options before they buy.

Mostly, companies are peddling variations on term-life insurance, which simply pays a death benefit to your beneficiaries if you die. But one discount broker, Charles Schwab, is also offering a universal-life policy (which features an investment account as well as a death benefit) and a second-to-die plan (or permanent cash-value coverage that insures two lives and makes a payment following the death of the second person).

Most commercial banks, which now sell about one-fifth of all annuities, aren't marketing traditional life insurance yet. But they're eager to begin. Thanks to a Supreme Court decision last March regarding Barnett Banks in Florida, the likes of Citicorp and First Union will soon be able to offer policies in most states. The court's ruling that a state cannot prevent national banks from selling insurance in towns with as many as 5,000 residents negates prohibitions on bank insurance sales in almost 20 states. It also allows banks to use regional offices to sell policies across the U.S. as state

regulators permit. At least one major insurer, Metropolitan Life, has said it is seriously considering selling its products through banks.

MetLife is one of many insurers investigating alternative channels to reach baby boomers, who have shied away from traditional life insurance. "Everyone's experimenting to figure out what

will work," says Bob Baranoff,

head of the specialty distribution services unit for LIMRA International, a life-insurance trade association. U.S. sales of all types of individual policies have fallen 30% since 1985, to 12 million last year, according to LIMRA. Unlike their parents, who purchased universal-life and other types of cash-value policies, baby boomers tend to save through 401(k) plans and individual retirement accounts. When they

buy life insurance, it's more likely to be term.

Insurers and marketers are responding to consumer demand by offering a variety of low-cost term-life products. Indeed, someone shopping for a basic term policy today can turn up more than a dozen fairly comparable choices simply by dialing a handful of 800 numbers or browsing a few Web pages on the Internet.

Of course, direct marketers such as Veritas (800 552-3553) have used toll-free numbers to provide policy quotes and plans for a decade. What's happening now is more players are involved, and they're teaming up in unusual ways. Not surprisingly, the Internet is a popular proving ground.

FAST AND FREE. In June, Intuit, maker of the popular personal-finance software Quick- en, announced that its new subsidiary, Interactive Insurance Services, is joining with



three major carriers, MetLife, Lincoln Benefit Life, and Zurich Direct, on a Web called InsureMarket at www.insuremarket.com. By summer's end, consumers should be able to get price quotes and sign up for Lincoln

Zurich term-lives.

Another online service, QuickQuote, had a site on the Web (<http://www.quickquote.com>) for a year, nabbing surfers with instant quotes on premium policies that run 5, 10, 15, or 20 years. If you purchase one, you provide your name, address, age, and annual income, and Incline Insurance Co. (Nev.)-based QuickQuote, which charges a commission on sale, sends an e-mail notification in the mail. The services aren't available to cyberspace. In May, Charlotte-based First Union has been stuffing its

What to Ask When Term Policy Shopping

- What are the terms of renewal when the original policy expires? For how long can it be renewed? Can I be denied lower rates at renewal based on the results of my medical exam? What will the new premium be?
- Is the term insurance convertible to permanent coverage (whole life, universal life, variable life)?
- Is this a level-term policy, meaning the premiums are guaranteed to stay the same for the life of the policy?
- Are the insurer, agency, and agent licensed to sell in my home state? (Check with your state insurance office for a definitive answer.)
- Have I been quoted "preferred rates" (the cheaper premiums that require superior health)? What are the criteria for preferred rates? For example, if I'm being treated for hypertension, will the insurer cover me at low premium?



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S. The problem
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For example,
lectQuote, a San
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ote offer a 10-
50,000 term poli-
Jackson Nation-

al Life Insurance for a level
premium of \$300. But what if
you are 57 years old and want
to convert to permanent cover-
age when the term's up? At
this premium, on this policy,
you wouldn't be allowed to do
that. You'd have to opt for a

more expensive (\$340 annual
premium) version of the same
policy—or a different one. "It's
not tough to decide you want
life-insurance coverage. But
choosing the right type isn't
as simple as it seems," says
Elliot Lipson, an Atlanta-
based, fee-only financial plan-
ner and insurance adviser.

Most sellers offer assis-
tance in figuring out the
amount and type of coverage
you should get. But they may
not explain the nuances—un-
less you ask. For example, if
you're considering different
term policies and you know
you want to renew when the
coverage period is up, com-
paring premiums alone is not
always the best way to as-
sess cost. Take North Ameri-
can's Premier Econo 10-year
Term. If you bought it at age
40, with a death benefit of
\$250,000, the premium would
be \$305, guaranteed for 10
years. When the term expires
and you want to renew, the
new premium would be
\$575—provided you're healthy
and you pass a medical exam.
If you develop health prob-
lems, you could be switched
to an annual renewable-term
policy at a cost of \$1,145 the
first year and \$1,250 the next.
"If you are concerned about
not qualifying for lower rates

at renewal, then you might
consider a policy that offers
reasonable guaranteed rates
at renewal," says Lipson. Or,
consider a policy that doesn't
require medical requalification.
Such a policy might be more
expensive at first, but over
time it could cost less if your
health deteriorates.

NEW TERRITORY. When pick-
ing a policy from a quote ser-
vice's list, check each insurer's
financial health with a ratings
service such as A.M. Best.
You want a carrier with
strong ratings and a reputa-
tion for treating customers
well. Internet shoppers
should also know that selling
on the Net is new territory
for insurers and regulators.
SelectQuote Vice-President
Steven Stark says its site
(www.selectquote.com) isn't
active yet because of con-
cerns that cyberselling does-
n't meet all regulations in
states where the company
does business.

If you're buying via an In-
ternet service, David Blair,
Ohio's insurance warden, ad-
vises you to confirm that the
insurance agency, agent, and
underwriter are licensed in
your home state. Otherwise,
if the insurer fails, you won't
have access to your state's
guarantee funds, which are
set aside to indemnify
policyholders. Or, say
you buy a policy from
an unlicensed agent, you
make a claim, and the
insurer won't pay. The
usual recourse would
be to appeal to your
state's insurance depart-
ment. But in this case,
your state would not
have jurisdiction. "Even
before the Internet, we
had fraudulent opera-
tors, and this medium
is rife for fraud," he
notes.

The result of these
burgeoning options in
term-life coverage is
more low-cost choices.
But unless you know
what you're buying,
there's still no insur-
ance you'll get the best
deal. *Lisa Sanders*

A Comparison of Offerings

A 40-year-old nonsmoking man who is 6 feet, 180 pounds
and lives in Illinois wants a 10-year renewable level-premium
term policy with a \$250,000 death benefit.

Here are some quotes from direct marketers:

COMPANY	POLICY	ANNUAL PREMIUM
QUICKQUOTE 800 628-3317 http://www.quickquote.com	• AIG Megaterm	\$297
	• Jackson National Prime 10-Year Term	300
	• North American Premier Econo 10-Year Term	305
	• First Colony Life Colony 10	307
	• First Penn-Pacific GTO 10	310
CHARLES SCHWAB 800 542-LIFE	• Great-West Life & Annuity Schwab 10-Year Life	335
SELECTQUOTE 800 343-1985	• CNA Life—Super Low Cost Term 10	288
	• Jackson National Prime 10-Year Term	300
	• Midland Life Alternative ST 10-Year	303
	• North American Premier Econo 10-Year Term	305
	• The Travelers Special T 10-Year Level Term	328

DATA: COMPANY REPORTS

TEQUILA TO SAVOR LIKE COGNAC

True or false? Tequila tastes like firewater, induces hallucinations, and must be guzzled in shots or mixed in a candy-sweet drink to disguise its flavor. An intoxicated little worm has settled to the bottom of every bottle. And, oh yes, this Mexican moonshine is a decidedly downscale beverage.

Fine tequila is none of these things. In fact, while the spirit evokes memories of frat house parties—and hangover hell—“super premium” tequila is fast gaining acceptance as a classy liquor that can be sipped in the manner of cognac, says Lucinda Hutson, author of *Tequila! Cooking with the Spirit of Mexico*, (\$16.95, Ten Speed Press). No wonder spirits-maker Sauza has been running advertisements with the tag line: “Life is harsh. Your tequila shouldn’t be.” Better tequilas also lead to superior margaritas, which remain the drink of choice for most tequila lovers. “It is important that people understand how versatile a spirit it is,” says Hutson.

MACHO. All tequila is extracted from the heart of the blue agave plant, which flourishes in the Mexican state of Jalisco. Although it has spiny, razor-sharp *penes* that make it resemble a pineapple, the blue agave is a member of the lily family. (Fiery mezcal, which often does have a worm in the bottle, is derived from another type of agave.) To be considered tequila, the Mexican government requires that at least 51% of fermentable sugars come from the blue agave.

SPIRITS

Even though definitions are fuzzy, tequila dubbed super premium is often made with 100% blue agave and bottled in Mexico. It is generally the most expensive, with prices of \$30 a bottle on up. Despite its macho reputation, at 80 proof, tequila has no more alcohol than standard gin, vodka, or rum.

The Mexican government established four distinct styles of tequila. Tequila *blanco* or *plata* (white or silver) most often comes fresh from the still and is clear, though some may “rest” in wood or steel tanks for up to 45 days. It can be pleasant by itself, or as part of a mixed drink. At Tapika, a Manhattan restaurant featuring Southwestern cuisine, a friend and I liked El Tesoro de Don Felipe Silver (about \$33 a bottle at retail), a very smooth brand with a hint of black pepper and spice. We preferred it to the silver Chinaco (\$35), which, like El Tesoro, is distributed by Robert Denton & Co. But unlike the two we sampled, some silver tequilas are coarse and may remind you of petroleum.

Gold tequila is essentially silver tequila that has been

Types of Tequila

WHITE OR SILVER At its best, this crystal-clear spirit can be sipped alone, especially when ice cold.

GOLD Often flavored with caramel, gold tequilas are popular for shooters, margaritas, and mixed drinks.

REPOSADO (RESTED) Oak aging for less than a year tempers the harshness of the flavor, which is excellent for sipping and mixed drinks.

ANEJO (AGED) Aged at least a year in oak barrels, fine *añejos* are similar to premium cognacs.

DATA: TEQUILA! BY LUCINDA HUTSON



THE SUPER PREMIUMS: Smoother, with subtle flavors

colored with caramel or other flavorings. At Tapika, we tried José Cuervo Especial, commonly known as Cuervo Gold, the best-selling tequila brand in the U.S. I found it way too rough to drink straight up, which is why it often resides in a margarita. As my friend put it: “There’s a reason people down shots of this.”

“MEDICINAL.” Many super premium tequilas fall into the other two classifications. Those that have “rested” in

oak tanks or barrels for two months to a year receive the *reposado* designation. Mexicans favor this young tequila taste, which works well as a shooter or sipping spirit, but one BUSINESS WEEK tester found the silver Patrón “medicinal and harsh.” I’m partial to the *añejos*, which have been aged in oak for a year or more and are best savored in a snifter. In Mexico, good *añejos* are drunk straight up in tiny shot glasses, and almost never wasted in a margarita. Aging helps the

tequila smooth over harsher edges. China Tesoro, Herradura, and Patrón all have strong in this category.

Some pricey tequilas are exceptional. The 100% agave, 3-year-old Reserva Familia José Cuervo introduced in a limited (4,000 bottles) to celebrate the 200th anniversary of the Cuervo brand. It costs \$75 for a standard corked and wax-sealed bottle—roughly double the price of top-quality *añejos* by command. The oily spirit compares favorably with cognac, and was a winner among BUSINESS WEEK testers.

Many of us also enjoyed the \$34 Sauza Tres Cicones, another cognac-like tequila with a buttery finish that is aged eight years in oak barrels. The aroma reminded me of “the hot wood of a sauna,” and another taster of “smooth summer breeze.” But best of all, by drinking only top-flight tequila, one had to extinguish the fires.

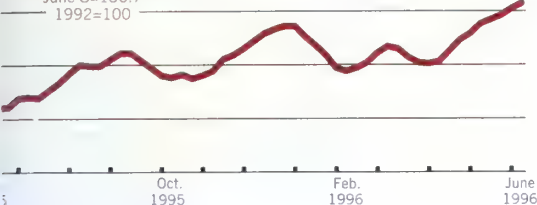
Edwina

Business Week Index

PRODUCTION INDEX

Change from last week: +0.4%
Change from last year: +8.3%

PRODUCTION INDEX
June 8=130.7
1992=100



The production index rose 0.4% in the week ending June 8. Before calculation of the 4-week moving average, the index also increased 0.4%, to 131.9 from 131.5. The index rose mainly because of gains in steel, trucks, lumber, and rail traffic. Offsetting production declines in autos, coal, paper, paperboard, and refining. Electric power output was unchanged.

The index will be unavailable for an indefinite period.

Source: McGraw-Hill Construction Information Group

FINANCIAL INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
PRICES (6/14) S&P 500	665.85	673.31	21.7
BOND YIELD, Aaa (6/14)	7.93%	7.81%	5.7
RAW MATERIALS PRICES (6/14)	106.9	107.7	-6.6
STOCK FAILURES (6/7)	NA	NA	NA
CREDIT LOSSES (6/5) billions	\$505.9	\$504.5r	4.5
SUPPLY, M2 (6/3) billions	NA	NA	NA
CLAIMS, UNEMPLOYMENT (6/1) thous	354	345	-5.6

Source: Standard & Poor's, Moody's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
GOVERNMENT FUNDS (6/18)	5.27%	5.24%	6.00%
DISCOUNT RATE (6/18) 3-month	5.50	5.49	5.94
RATES OF DEPOSIT (6/19) 3-month	5.46	5.47	5.91
MORTGAGE (6/14) 30-year	8.57	8.45	7.82
FIXED RATE MORTGAGE (6/14) one-year	6.15	6.01	5.98
LIBOR (3-month) (6/19)	8.25	8.25	9.00

Source: Federal Reserve, HSH Associates, Bloomberg Financial Markets

1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

HOME SALES

June 25, 10 a.m. EDT ▶ Existing homes are being sold at an annual rate of 4.13 million in May, says the median forecast of economists surveyed by MMS International, a McGraw-Hill Companies. Sales had risen for three months in a year, ending a 0.5% gain in April, to 4.13 million. Housing remains resilient despite higher mortgage rates. Part of the rebounding California market, offsetting weakness elsewhere.

CONSUMER CONFIDENCE

June 25, 10 a.m. EDT ▶ The Conference Board's index of consumer confidence edged slightly higher in

June, rising to 102 from 101.2 in May. In May, the expectations component of the index fell sharply as more consumers worried about job prospects over the next six months. Still, confidence in general has been at a high level this year, suggesting that shoppers are not about to cut back on their spending.

DURABLE GOODS ORDERS

Wednesday, June 26, 8:30 a.m. EDT ▶ The MMS median forecast calls for an increase of 1% in durable goods orders in May. Orders declined by 1.9% in April, dragged down by a steep falloff in the volatile aircraft sector. However, new orders for capital goods, excluding aircraft, have started to

drift lower. That's a sign that the capital-spending boom may be winding down. Unfilled orders probably increased in May, after falling 0.2% in April.

UNEMPLOYMENT CLAIMS

Thursday, June 27, 8:30 a.m. EDT ▶ New filings for state unemployment benefits probably fell to 350,000 for the week ended June 22. Claims continue to fall lower after spiking up during the March strike at General Motors Corp. In the first week of June, claims stood at 360,000. With the bond market worried that faster wage growth will become inflationary, economists are looking at jobless claims for hints of any slack in the labor markets.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (6/15) thous. of net tons	2,051	2,056#	4.3
AUTOS (6/15) units	143,250	144,048r#	8.9
TRUCKS (6/15) units	123,132	130,052r#	4.9
ELECTRIC POWER (6/15) millions of kilowatt-hrs	66,360	62,646#	7.7
CRUDE-OIL REFINING (6/15) thous. of bbl./day	14,252	14,405#	-2.2
COAL (6/8) thous. of net tons	19,828#	18,711	9.4
PAPERBOARD (6/8) thous. of tons	886.0#	884.9r	-4.7
PAPER (6/8) thous. of tons	817.0#	806.0	-4.2
LUMBER (6/8) millions of ft.	469.0#	395.5	6.2
RAIL FREIGHT (6/8) billions of ton-miles	25.5#	23.1	5.8

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPAl, SFPAl, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (6/19) \$/troy oz.	386.300	384.800	-1.0
STEEL SCRAP (6/18) #1 heavy, \$/ton	136.50	138.50	-2.8
COPPER (6/15) ¢/lb.	112.5	114.5	-19.8
ALUMINUM (6/15) ¢/lb.	70.3	71.8	-16.6
COTTON (6/15) strict low middling 1-1/16 in., ¢/lb.	81.67	81.68	-23.9
OIL (6/18) \$/bbl.	21.26	20.02	18.0

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (6/19)	107.97	109.46	84.52
GERMAN MARK (6/19)	1.52	1.54	1.40
BRITISH POUND (6/19)	1.54	1.53	1.60
FRENCH FRANC (6/19)	5.16	5.21	4.88
ITALIAN LIRA (6/19)	1535.2	1550.3	1630.3
CANADIAN DOLLAR (6/19)	1.37	1.37	1.38
MEXICAN PESO (6/19) ³	7.522	7.564	6.250

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

BusinessWeek **ONLINE**

Sunday

Oracle is on the leading edge of the drive to market the Network Computer—an information appliance that could bring cyberspace to the masses. Join Oracle CEO Larry Ellison and Rob Hof of BW's San Francisco bureau to hear all about it. **June 23**

9 p.m. EDT in the Globe

Wednesday

Technology can backfire on the human race, and author Edward Tenner tells how in his new book, *Why Things Bite Back*. From the Titanic to DDT to carpal tunnel syndrome, he will talk about unintended—and sometimes alarming—consequences.

June 26

9 p.m. EDT

BW Online Chat Room

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event

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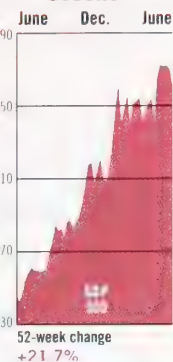


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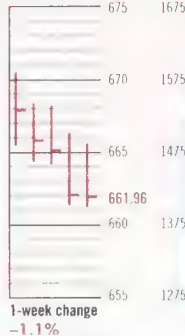
STOCKS

in the copper market
stocks and bonds from
ines. Sumitomo Corp.
hat a former head of cop-
g may have lost them an
\$1.8 billion over 10
per prices plunged. The
bond markets had a
k as well. Tech stocks fell
n that growth in the com-
stry would slow. Inflation
inued to roil the bond
ending the yield on the
easury to 7.19%—a 13-
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11%.

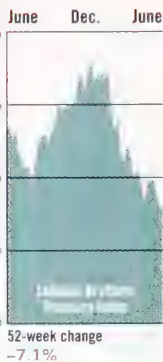
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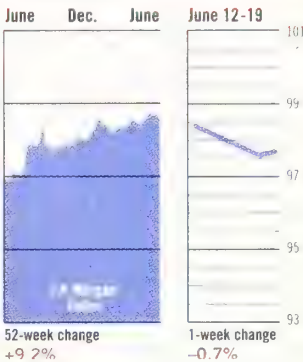
BONDS



BONDS



THE DOLLAR



MARKET ANALYSIS

INDEXES	Latest	% change	
		Week	52-week
S&P INDUSTRIALS	5648.4	-0.4	24.2
COMPANIES (S&P MidCap Index)	236.6	-2.0	19.5
COMPANIES (Russell 2000)	347.2	-3.5	22.8
COMPANIES (Russell 3000)	378.8	-1.4	22.2
STOCKS	Latest	% change (local currency)	
		Week	52-week
FINANCIAL TIMES 100)	3753.2	-0.4	11.1
Nikkei Index)	22,367.4	1.2	49.6
(TSE COMPOSITE)	5072.7	-0.4	12.0

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.23%	5.25%	5.56%
30-YEAR TREASURY BOND YIELD	7.11%	7.19%	6.54%
S&P 500 DIVIDEND YIELD	2.16%	2.13%	2.45%
S&P 500 PRICE/EARNINGS RATIO	19.1	19.2	16.7
TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	625.0	622.5	Positive
Stocks above 200-day moving average	60.0%	62.0%	Neutral
Speculative sentiment: Put/call ratio	0.68	0.59	Neutral
Insider sentiment: Vickers sell/buy ratio	2.31	2.24	Neutral

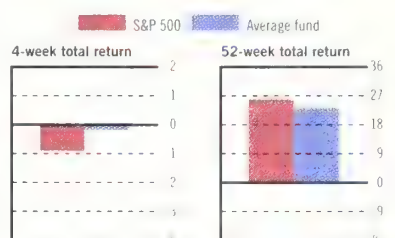
BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

WITH LEADERS	% change		Strongest stock in group	% change		Price
	1-month	12-month		1-month	12-month	
FACTURED HOUSING	14.4	47.6	FLEETWOOD ENTERPRISES	14.4	49.1	30 3/4
RE TIME	9.1	34.4	BALLY ENTERTAINMENT	21.2	167.7	29 1/4
	7.5	84.1	REEBOK INTERNATIONAL	10.1	-7.8	32 3/4
CD	7.0	34.9	PHILIP MORRIS	7.5	39.2	102 1/2
S AND MOTELS	6.7	35.7	HILTON HOTELS	15.1	79.6	119 1/2
WITH LAGGARDS	% change		Weakest stock in group	% change		Price
	1-month	12-month		1-month	12-month	
MINING	-11.2	3.6	NEWMONT MINING	-14.7	12.4	49 1/2
TER SYSTEMS	-9.6	12.6	DIGITAL EQUIPMENT	-21.0	-1.4	44 1/4
SHINGS AND APPLIANCES	-8.9	1.5	WHIRLPOOL	-12.1	-12.1	50 1/2
NE TOOLS	-8.9	-10.4	CINCINNATI MILACRON	-10.2	-14.0	23
S	-8.8	16.4	ASARCO	-13.0	0.0	29 1/4

MUTUAL FUNDS

LAGGARDS				
Four-week total return	%	United Services Gold Shares	-12.9	
	%	Invesco Strategic Gold	-12.0	
	%	Bull & Bear Gold Investors	-12.0	
52-week total return	%	Steadman Technology	-21.4	
	%	Steadman American Industry	-13.5	
	%	United Service Gold Shares	-10.8	



RELATIVE PORTFOLIOS

portfolios represent the
value of \$10,000
one year ago
portfolio
figures indicate
total returns

U.S. stocks
\$12,458
-1.33%

Foreign stocks
\$11,731
+1.68%

Money market fund
\$10,535
+0.11%

Gold
\$10,093
-0.45%

Treasury bonds
\$9,910
+0.55%

This page is as of market close Wednesday, June 19, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as

of market close June 18. Mutual fund returns are as of June 14. Relative portfolios are valued as of June 18. A more detailed explanation of this page is available on request. r=revised

THE U.S. IS BECOMING A GLOBAL NAG

America is in danger of becoming a global nag. Everywhere you turn, there is Washington wagging its finger at friends and foes alike. Are the Germans or French trading with that old Communist in Cuba? We'll lock them up if they try to take their kids to Disneyland. Building a dam for electricity and flood control in China? Uh oh, that will hurt the environment, so no Ex-Im Bank financing for U.S. companies. Human rights. Child labor. Netting dolphins. Nontariff barriers. Tech transfer. All worthy causes, perhaps. But by complaining about everything and everyone, America risks becoming a global busybody rather than a world leader. When even friends like Canada and Britain protest, something clearly is wrong.

Take the Helms-Burton Act, a unilateral trade sanction passed by Congress in March after Cuban jets shot down two unarmed civilian planes. Helms-Burton permits lawsuits in U.S. courts against foreign companies and their executives if their business with Cuba involves expropriated property. The law blocks these foreign executives from entering the U.S. All of this, of course, violates the North American Free Trade Agreement and World Trade Organization rules.

Helms-Burton is an election-year sop by politicians to Florida's Cuban voters. Trying to force allies to carry out secondary boycotts is a truly dumb way of executing foreign policy. Congress is readying a similar law for Iran and Libya. As the world's superpower, the U.S. has an obligation to set international rules. But if the U.S. becomes a global scold, it will lose the support of the very people it needs to achieve its goals. America must focus on key issues and forge multilateral alliances. Building a coalition with Europe to stop Iranian support of terrorists is more important than bludgeoning it with sham sanctions on Cuba. Getting the Chinese to curb software piracy is more important than criticizing them on their environment.

Foreign policy is about national interest, not social work. It is about strategic choices, not endless complaining. It is about coalition-building, not unilateralism. Congress must show more maturity and sophistication in global issues. And the President must show more leadership.

HELP WANTED: A NEW TRANSPORTATION HEAD

It's a nightmare come true. The Transportation Secretary promises on TV that "this airline is safe" following a horrible ValuJet Airlines Inc. crash killing 110 people. A month later, he admits he's wrong when the Federal Aviation Administration shuts ValuJet down for shoddy maintenance.

It's a mystery why it took so long for the FAA to discover safety problems at ValuJet. There certainly were enough problems to indicate something was wrong. BUSINESS WEEK recent-

ly disclosed that an engine overhauled in Turkey by a station that lacked FAA approval was the cause of a ValuJet 9 fire last year. There were problems that drew FAA attention to the airline. But the agency apparently didn't do its job.

Then again, the FAA does have two jobs—ensuring safety and promoting flying. Transportation Secretary Federico Peña was doing the latter when he praised low-fare carriers a month before the crash, mentioning ValuJet by name and vowed to continue to promote them. The FAA's failure to oversee ValuJet has finally shocked the regulatory agency into asking Congress to change its charter. It wants to focus solely on airline safety and let the airline industry promote itself. It shouldn't have taken a terrible crash to force the FAA to realize it needs all its resources to regulate a changing industry that is outsourcing maintenance all over the world. Congress should grant the request immediately.

But that is not enough. Anthony J. Broderick, the FAA's safety watchdog, is retiring as of July 1. Peña should step next. He has lost all credibility with the flying public. The new FAA needs a new Transportation Secretary.

DON'T GIVE RUSSIA THE COLD SHOULDER

Unfashionable as it may sound in election-year Washington, it is time for the U.S. to come seriously to the aid of Russia. For the first time in their 1,000-year history, Russians are freely voting for a President. And for the second time in this century, Russia is on the brink of joining the free market economy. These epic developments are being met with blasé indifference by a self-absorbed America increasingly unable to show leadership on the world scene.

As George F. Kennan, the man who coined "containment," points out in *At a Century's Ending*, eight decades ago Russia was poised to become a "normal" European nation. It had a Parliament, foreign investment, and a growing market economy. A communist *putsch* in 1917 reversed a drive for modernization and sent Russia back to a traditional totalitarian government, centralized economy, and an overseas empire.

With the end of the cold war, Russia joined the world again in 1989 and America immediately benefited. U.S. defense spending was cut and its children could sleep at night without fear of nuclear war. We accept this state of affairs without question today. But we shouldn't. Had the Communist Gennady Zyuganov won the recent election (he still has a slim chance in the second round of voting), Russia would have reverted for a second time in the 20th century to totalitarianism, economic autarky, and empire building.

Boris Yeltsin will need a great deal of support to win out of the next round of voting. The U.S. has a strategic interest in helping Russia continue on its path toward a free-market democracy. With the aid of its allies, America should help Russia the way it helped Germany and Japan after World War II. Nothing could be more in America's interest—or in Russia's.

SS WEEK
uly 8



BusinessWeek

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ECONOMIC

Don't be fooled by today's strong statistics. And don't be suckered by political rhetoric. America needs faster growth. Here's how to get it.

GROWTH

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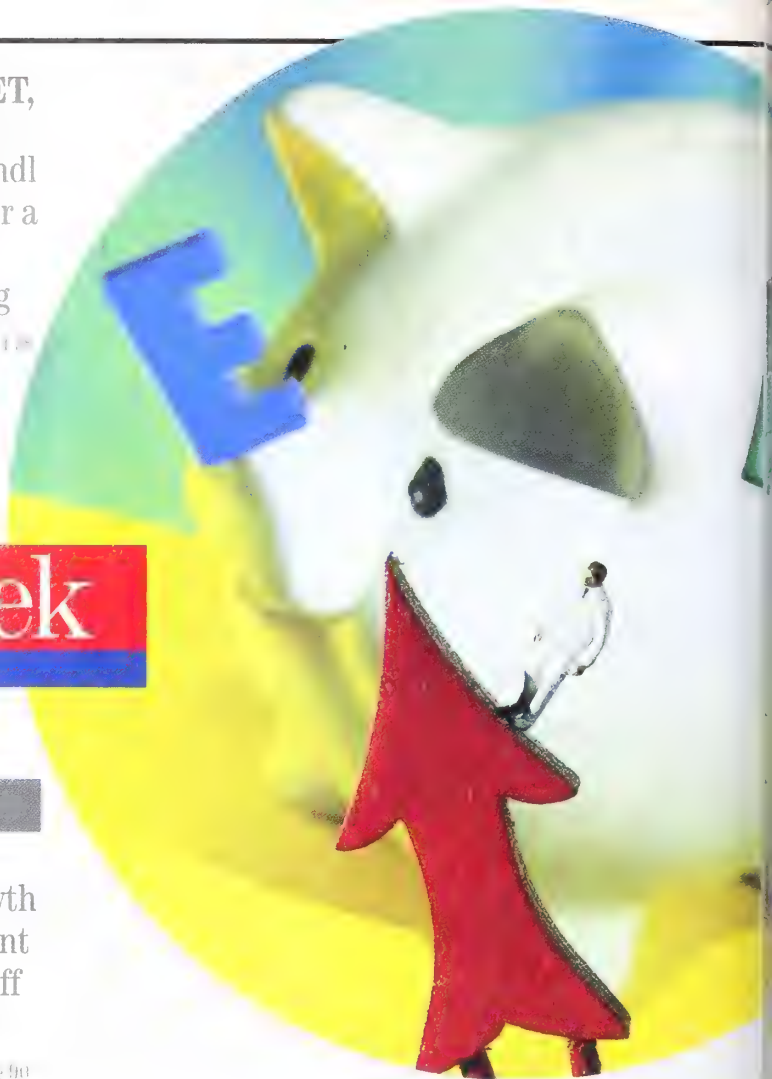
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**READY, SET,
DEVOUR**
AT&T's Mandl
is aiming for a
third of the
local calling
market *page 115*



BusinessWeek

JULY 8, 1996

COVER STORY

LET'S GET GROWING

Raising the long-term growth rate by one percentage point could bring a massive payoff in wages, living standards, and economic security *page 60*

Cover Story

90 ECONOMIC GROWTH: A PROPOSAL

Employment is surging, the stock market is strong, and corporate profits are up. So what's wrong with this picture? Since the mid-1970s, growth has plodded along at a 2% or so a year. These lukewarm gains aggravate nearly every social problem plaguing the country. But the U.S. can achieve faster economic growth—and higher living standards—without fueling inflation. Here's how to make it happen

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Such a thing wasn't supposed to happen anymore, but it has: The chip industry suffers its worst downturn in years

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WORLD CROWN

For the first time, a U.S. company, GE, tops BW's Global 1000 page 46



BIG SWINGS

Stocks may seem riskier than bonds. But are they? page 108

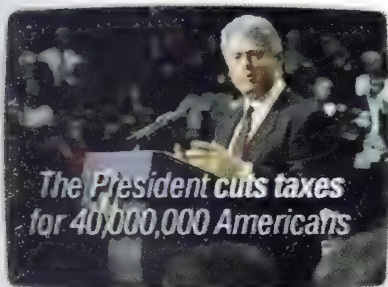
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THRILLS, THEN CHILLS

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FIRST STRIKE

Clinton's early ad blitz is coopting issues important to voters page 126



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Yes, growth can be speeded up
Time for Congress to get cracking

Up Front

EDITED BY LARRY LIGHT

ECONOMIC ANGST

TAKE MY JOB, PLEASE!

GIVEN A CHOICE BETWEEN A job and a pink slip, most people would take the job, right? Not employees of First Interstate Bancorp, recently acquired by Wells Fargo. A bunch of them are clamoring to be laid off because the severance packages are so lush.

This is a headache for Wells Fargo, which expects its recent takeover of First

Interstate to result in some 7,200 job cuts. In scores of letters and calls to Wells management, employees not on the downsize list stress their poor performances, vacation needs, or desire for a nest egg, says the bank. At least a dozen have obtained legal counsel and are threatening to sue Wells for unfairly dol-



ing out severance checks to some, while retaining others. First Interstate created

these rich deals to protect employees from a takeover. That didn't dissuade Wells, which previously expected to pay \$270 million in severance—and now says the figure will be much higher. For person, the outlay is twice as generous as the bank's normal severance package. Wells must offer at least one year's pay for some laid-off managers, and as much as two years' to others, depending on tenure. Lower-ranked salaried employees get four weeks for every year's service. *Linda Himelstein*

PLASTIC FANTASTIC

A CRACKABLE NEST EGG?

THE CHORUS OF SKEPTICISM greeting the new 401(k) credit card is deafening. But Banc One's product, which lets you tap your tax-free 401(k) retirement account for day-to-day expenses, has apparently passed regulatory muster.

According to the bank, the Internal Revenue Service has informally told it there won't be any move to squelch the thing. Reason: Banc One will require that cardholders repay each month's loans within five years, which satisfies

market the card this fall. Critics say that card borrowing is for short-term consumer needs, which is anathema to long-term retirement planning. Stephen Brobeck, executive director of the Consumer Federation of America, warns that 401(k) accounts may end up depleted. "Businesses have a responsibility not to market dangerous products." *Mike McNamee*

NEW WORLD ORDER

ON THE MARCH AGAIN IN GDANSK

THE GDANSK SHIPYARD, birthplace of the Solidarity movement, is a hot issue for Poland's government, led by ex-Communists. President Aleksander Kwasniewski, who heads the Democratic Left Alliance party (SLD), has



SOLIDARITY: Strikes loom

forced the operation to file for bankruptcy. Irony: The former Marxists point to other restructured Polish shipyards as models—because they are profitable.

The government, which owns 60% of the ailing shipyard, has made 5,000 Gdansk workers take a two-month leave. Now, the shipyard loses up to \$7 million per ship. Hoping to show Western lenders it's serious about free-market reforms, the government wants to axe Gdansk's subsidies and lease it to a company that will pare its workforce by two-thirds.

The Solidarity union, an opponent of the SLD and of layoffs, views the yard closing as political revenge. It organized a large worker march in Warsaw to protest the bankruptcy. During the presidency of Solidarity founder Lech Walesa, ousted by Kwasniewski in last December's election, subsidies were copious to Gdansk and other money-losers. *Peggy Simpson*

THE LIST BEER BLOAT

Wall Street's recent thirst for microbreweries' initial public offerings made for heady, if short-lived, valuations. Such fad stocks "get a speculative froth," says Kathleen Smith, an analyst at Greenwich (Conn.)-based Renaissance Capital.



Trouble is, small-time brewmeisters often don't have the marketing heft to grow with the speed that keeps investors happy. The market sobered up when it saw unspectacular earnings (Redhook Ale) or outright losses (Frederick).

MICROBREWERY IPOs: THE FIZZ IS GONE

COMPANY NAME (Date Went Public)	OFFERING PRICE	CURRENT PRICE*	HIGHEST PRICE
PETE'S BREWING (11/07/95)	18	18	27½
REDHOOK (08/17/95)	17	22½	35
BOSTON BEER (11/20/95)	20	21½	33
HART BREWING** (12/14/95)	19	11½	22½
MENDOCINO BREWING (2/16/95)	6	10½	10½
MINNESOTA BREWING (10/26/93)	4½	5¼	8¾
FREDERICK BREWING (03/11/96)	6	5¼	7¼

*As of 06/24/96.

**As of 07/01/96, Hart Brewing became Pyramid Breweries
DATA: RENAISSANCE CAPITAL



OK: 401(k) loans may sail

the tax code. Beyond that period, any loan from a 401(k) plan is taxed. Also, says tax attorney Mark Wintner of Stroock & Stroock & Lavan, there are no legal restrictions on what a 401(k) loan must be used for. The IRS won't comment.

The Columbus (Ohio) superregional bank aims to test-



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"Absolute Best New Car Value"
-CarSmart 1995 Summer Edition

1995 "Best Buy"
-Chicago Tribune, 6/11/95

1995 "Best Buy of the Year"
-Carguide

1995 "Design and Engineering" Award
-Popular Mechanics

"Best Luxury Sedan"
-1995 MotorWeek Drivers' Choice Award

Luxury Car of the Year
-Motoring '95

Top Ten All American
-AutoWeek

"Interior of the Year" Luxury Category
-Inside Automotives

1996 "Total Quality Award" in its class
-Strategic Vision, Inc.

"America's Finest"
-Playboy Magazine

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Chicago Tribune, 6/11/95 "Strategic Vision's™ 1995 Vehicle Experience Study is based on a total of 31,440 new vehicle buyer responses indicating owner's positive and negative experiences during the first 90 days of ownership. "Strategic Vision's 1996 Vehicle Experience Study™ surveyed 35,652 Oct.-Nov. new vehicle buyers of 200+ models during the first 90 days of ownership. Lease: \$399 per month for 36 months. **\$2,600 DOWN PAYMENT.** \$3,448.33 due at lease signing (first month's payment of \$398.33, plus \$450 refundable security deposit, plus down-payment). Taxes, license, title fees, and insurance extra. GMAC must approve lease. Example based on Aurora model: \$35,500 M.S.R.P., including destination charge. Monthly payments total \$399.88. Payments may be higher in AL, CA, CT, HI, NY, RI, TX and VA. Option to buy at lease end at price determined at lease signing. Mileage charge of 15 cents per mile over 36,000 miles. Lessee pays for excess wear. You must take retail delivery out of retailer stock by 10/2/96. This is a special GMAC program. See your participating retailer for qualification details.

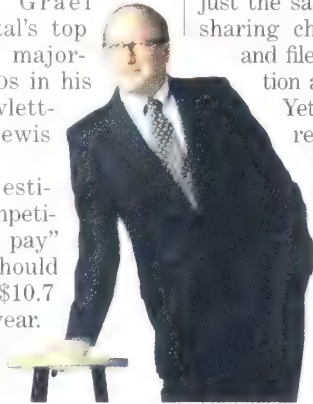
Up Front

HONCHOS

YES, VIRGINIA, THERE ARE UNDERPAID CEOs

YOU'VE READ PLENTY ABOUT the corporate fat cats pulling down vast sums. What about a CEO who's underpaid? Pay consultant Graef "Bud" Crystal's top pick among major-company CEOs in his survey: Hewlett-Packard's Lewis Platt.

Crystal estimates a "competitive level of pay" for Platt should have been \$10.7 million last year. Platt's pay totaled \$4.94 million, or 54% less. **PLATT:** *Getting half-pay?*



mum performance," Crystal says.

Unlike most CEOs, Platt doesn't get an annual bonus, just the same smallish profit-sharing check as HP's rank and file. And his stock-option awards are modest. Yet Hewlett-Packard's returns to investors bested all but 5% of the largest 500 companies in the past three years. BUSINESS WEEK's recent Annual Compensation Scoreboard gives him good marks, though not the best for shareholder return. Crystal

measures performance differently—adjusting for a company's size, among other things.

John Byrne

APPOINTED ROUNDS

THE POST OFFICE'S NEW MATH

THE U.S. POSTAL Service has launched a \$300,000 print ad campaign to show the first-class stamp is a bargain. But the Post Office needs to check its math.

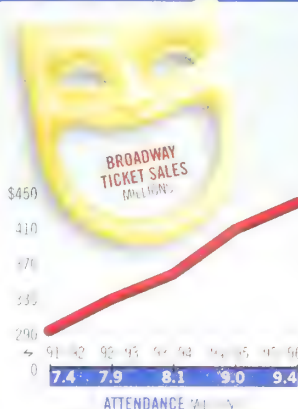
The ads, which ran in May, compare stamp price hikes—up from 3¢ in 1940 to 32¢ now—to those for a half-gallon of milk (25¢ to \$1.43) and a loaf of bread (8¢ to 79¢). Implication: Stamps rose less. "Postage rates remained well below the rate of inflation for that period—21% lower," says the ad.

Not quite. The stamp is up 967%, vs. 887% for the bread and just 472% for the milk. Overall inflation, 988%, barely outpaced the stamp. There

are 21 percentage points difference, but the gap really is 2.2%. Ad firm Young & Rubicam says it meant only that bread and milk hikes were comparable to the stamp's, not higher. It admits erring on the CPI.

Dean Foust

THE BIG PICTURE



DATA: LEAGUE OF AMERICAN THEATERS & PRODUCERS INC.

DRAWN & QUARTERED



AFTERLIVES

HE'S PUTTING YOUR MONEY ON YELTSIN

MICHAEL BLUMENTHAL HAS undertaken one of his riskiest ventures yet: investing in Russia. As chairman of the U.S. Russia Investment Fund, Blumenthal has a lot riding on Russia's upcoming runoff election.

To buoy Russian private enterprise, the former Treasury Secretary's fund, financed by federal money, has taken \$100 million worth of equity positions in 20 large companies and made \$7 million in loans to almost 100 smaller outfits since its 1994 debut. Beneficiaries range from U.S.



BLUMENTHAL: Antsy

corporations setting up shop there, such as PepsiCo, Russian businesses that include supermarkets, and mineral water and oil products. Dividends go to the fund's reinvestment.

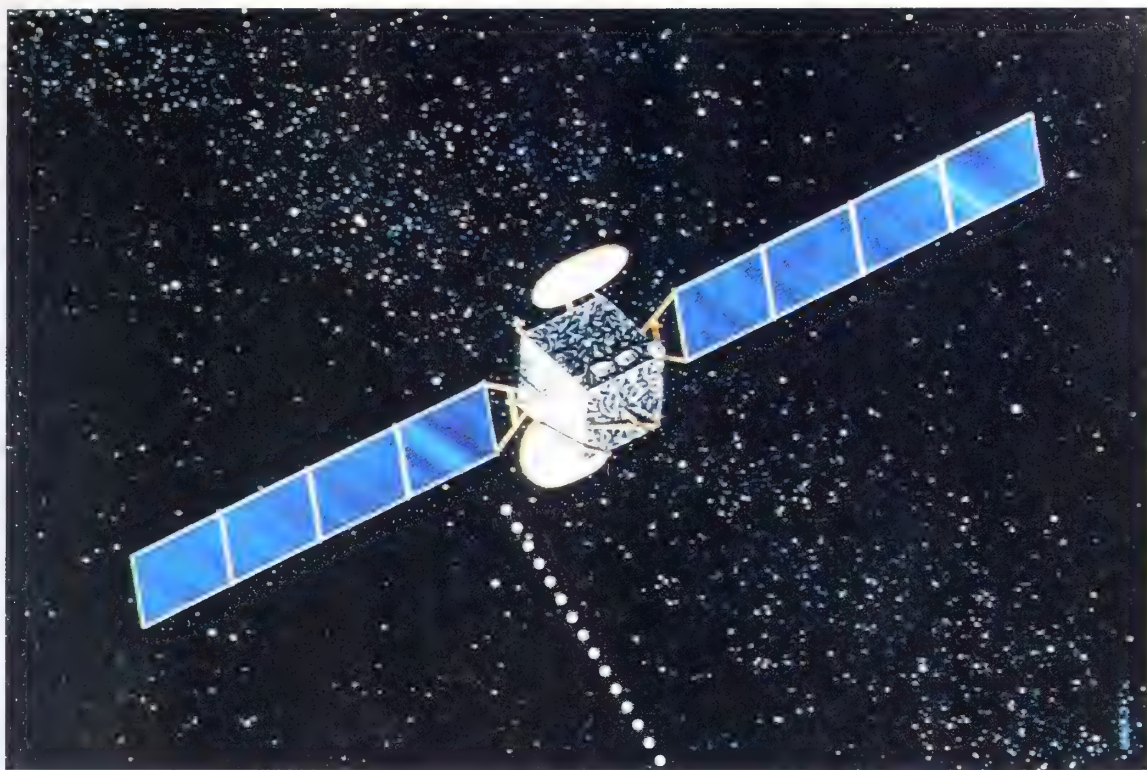
But if Communist candidate Gennady Zyuganov defeats President Boris Yeltsin, Blumenthal fears support for the fund's efforts could be in serious trouble. Blumenthal: "It makes a lot of difference."

Blumenthal, 70, has been in Russia since the fund began. In addition, he occasionally advises Treasury Secretary Robert Rubin on

transformation matters, following in what he calls an "informal tradition." A senior adviser at the Lazard Frères investment firm, he also is writing a book on European history.

Blumenthal knows about political and business difficulties firsthand. After serving as Bendis' CEO, he became President Jimmy Carter's Treasury chief. But he stepped down in 1979 when Carter, suffering in the polls, overhauled the Cabinet. Blumenthal then headed Brouhaha, overseeing its merger with Sperry to form computer maker Unisys. However, the company soon ran into trouble, and the beleaguered CEO left in 1990 to join Lazard. Randi Feigenbaum

FOOTNOTES Parents who say their kids should have their own credit cards by age 18: 64%

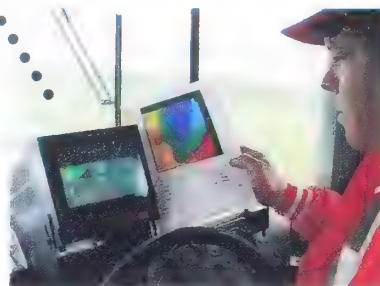


Space-age technology helps farmers make down-to-earth decisions.

If you can't imagine farmers using satellite technology, you're probably not alone. But that's farming in the '90s, precision farming, and it has planted the seed for a whole new era in farm management.

Through state-of-the-art Global Positioning Systems, farmers can gather new, detailed information about their fields. From that information, they can apply herbicides and pesticides with pinpoint-accuracy, using less chemicals more efficiently. That's a great way to protect the environment, and a more cost-effective way to get food to consumers.

So while this new farming technology might seem a little far-out, the results can be felt very close to home.



Supermarket to the world

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TPA MIGHT REALLY BE A MIRACLE DRUG

Thank you for "A miracle drug's second coming" (Science & Technology, June 3). On June 7, my wife's father had a stroke. My wife went with him to the hospital. I relayed your article's information about TPA to her by cell phone.

The emergency room staff was very surprised she knew about TPA: The doctor on call rarely used it. We strongly believe my wife's understanding of the pros and cons influenced the doctor to consider using TPA. After tests were done to confirm a clot rather than bleeding, TPA was administered slowly by IV. Initially, my wife's father could not move his left leg and arm at all. He had a severe facial droop on the left side. But within 24 hours of using TPA, all functioning on that side was back to normal.

His recovery has been very rapid. Did TPA facilitate the recovery, or would it have happened anyway? We don't know, but we believe TPA played a major part.

Charles Diestel
Park Ridge, Ill.

WHY CALIFORNIA NEEDS A NUCLEAR-WASTE DUMP

If the antinuclear crowd stops the Ward Valley radioactive-waste facility—and in turn bankrupts American Ecology Co.—California will take a bigger economic hit than anyone bargained for ("Nuclear waste with nowhere to go," News: Analysis & Commentary, June 10). Without a disposal facility, every extra dollar spent to store waste at our hospitals, labs, biotech firms, universities, manufacturers, and power plants is a dollar not invested in products and services.

The uses of nuclear technologies in California are responsible for 220,000 jobs, \$17 billion in business activity, and \$3 billion in tax revenues. It's senseless to risk these economic benefits when we have a site that has been li-

censed by the state and given a clean bill of health by the National Academy of Sciences and the California Supreme Court.

As a practicing physician in California, I want future generations to be able to enjoy the many benefits of clear medicine. Anti-Ward Valley forces are working against our state's economy and our quality of life.

Robert Carretta, MD
Chairman, Organizations United for Responsible Low-Level Radioactive Waste Solutions
Washington

There is plenty of time to come up with a more suitable site, a more sensible design, and perhaps an operator with a better track record and financial qualifications. American Ecology's difficulties may be a blessing to the people and the economy of California—an opportunity to avoid the possibility of contaminating a truly irreplaceable asset: our water supply.

Sheldon Plotkin and James C. Williams
Southern California Federation of Scientists
Los Angeles

NIKE: WHAT ABOUT THE SWEATSHOPS?

"The soul of a new Nike" (Marketplace, June 17), concerning Nike Inc.'s expansion into more of the sports-apparel business, failed to mention the sweatshop conditions under which Nike goods are produced. Nike's sales, profits, and stock price are booming, while the people who produce the products work for slave wages.

BUSINESS WEEK ought to expose the working conditions of workers employed by big corporations such as Nike. The public needs to be informed so they can decide whether they want to purchase goods produced under horrible conditions. Many Americans would boycott Nike products if they were made aware of the exploitation that people in Indonesia, Thailand, and Vietnam (to name just a few) are suffering. Profits should

Business Week

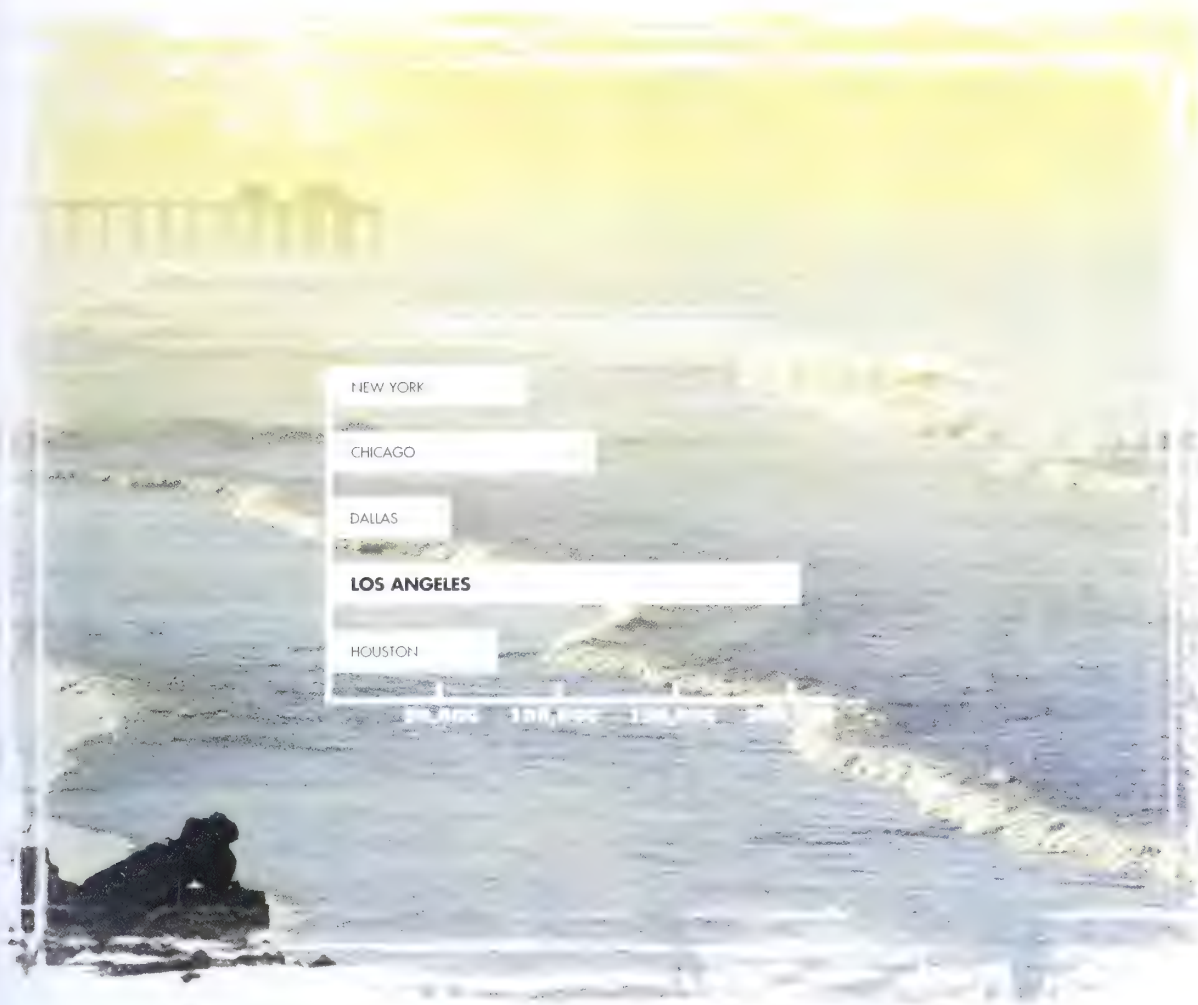
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CORRECTIONS & CLARIFICATIONS

"The New Hucksterism" (Cover Story, July 1) incorrectly said Hiram Walker & Sons hired actors to talk up Hennessy cognac in bars. Schieffelin & Somerset Co., Hennessy's U.S. importer, was responsible for the marketing campaign.

never take precedence over human rights and human dignity.

Anthony G. Stegman
San Jose, Calif.

ALTERED STATE FOR MICROSOFT

California has many fine software companies ("Microsoft's long march," International Business, June 24). But Microsoft is located not in Redmond, Calif., but up the coast in Redmond, Wash.

Richard McCracken
Chula Vista, Calif.

DEREGULATION WON'T BRING ON BLACKOUTS

"Who's watching the power grid?" (Science & Technology, June 17) implies that deregulation of the utility industry, already well under way, threatens

the reliability of service. BUSINESS WEEK should be cautious about accepting this myth, promoted by those who cling to pervasive government regulation.

Commonwealth Edison Co. had problems during a heat wave in July, 1995, but deregulation and the interstate high-voltage grid played no role. An investigation by Failure Analysis Associates, sponsored by the state of Illinois, found the causes to be aging low-voltage local distribution equipment, a deficient equipment-replacement program, and heat-related record demand for electricity.

Steven A. Mitnick, Director
Hagler Bailly Consulting Inc.
Arlington, Va.

THE FDA WAS AGITATED OVER HALCION

"How the FDA let Halcion slip through" (News: Analysis & Commentary, June 17) discloses the tip of the iceberg of the internal conflict and suppressed information at the Food & Drug Administration concerning the damaging effects of Upjohn Co.'s sleeping medication. Spontaneous reports flowing into the FDA have shown an unusually high association between Halcion and a syndrome that consists of "anger or rage, aggression, and some actual assaults and murders," according to an in-house

report by a member of the FDA's Epidemiology & Surveillance Div. That vision has shown far more concern about these potentially tragic findings than the agency officially acknowledged.

Peter R. Breggin, MD
National Director
Center for the Study of
Psychiatry & Psychology
Bethesda,

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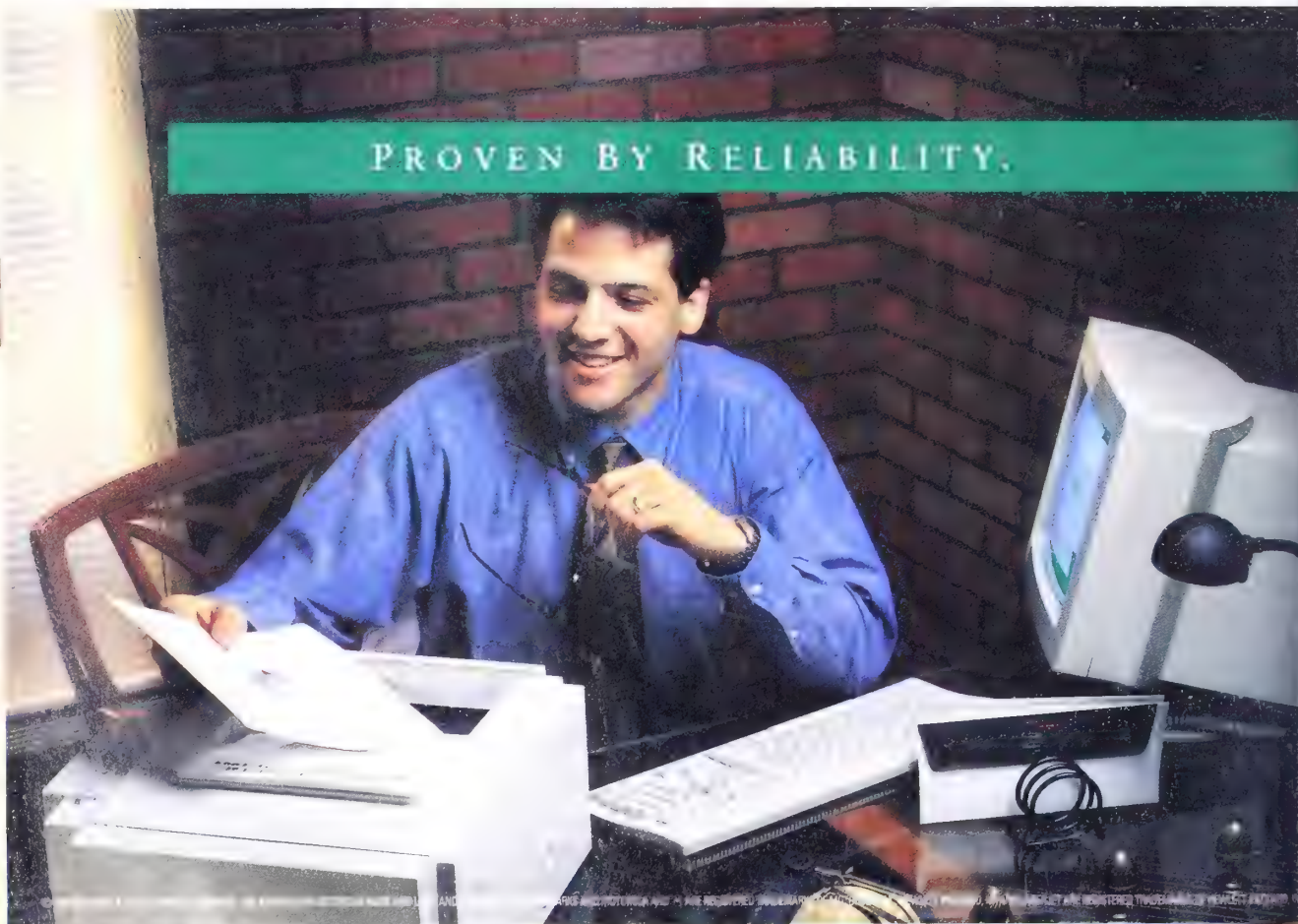
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Have you got your book? As
we head off to leisurely sum-
mertime pursuits, one thing
st of us require is a good read to
e along. So, in the spirit of the sea,
here is a sampling of current pa-
perbacks worthy of consideration.

Many of the most engaging business
times out now are also commentaries
on contemporary society. Consider Po-
nson's analysis in his novel **Bom-
bardi** (Penguin, \$11.95): "The infor-
mation economy was a Ponzi scheme
coming out of control. The investment
bankers got rich slaving away, so they
relied in their tax accountants... their



therapists... their divorce lawyers....
The doctors, [who] worried about being
sued by the lawyers, called their insur-
ance brokers for malpractice coverage."
Bombardi paints an outrageous pic-
ture of gonzo bond traders. Their lies,
schemes, addictions, and sales spiels will
have you guffawing—and, perhaps, nod-
ding in recognition.

Joseph Nocera's **A Piece of the Ac-
tion: How the Middle Class Joined
the Money Class** (Touchstone, \$14)
takes us back to the time, not so long
ago, before credit cards, mutual funds, or
discount brokers. These developments,
says Nocera, have given average Amer-
icans the passion for money manage-
ment once restricted to the very rich.

More important, says the author,
those millions have wrested much of
the control of the markets from
traders and mega-investors.

In **Silicon Snake Oil: Second
Thoughts on the Information High-
way** (Anchor, \$14), Clifford Stoll exam-
ines another popular pastime: the Inter-
net. But unlike Nocera, Stoll isn't
convinced that this is a development
worthy of enthusiasm. "A poor substi-
tute it is, this virtual reality where frus-
tration is legion and where... important

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aspects of human interactions are relentlessly devalued," he writes in this cautionary tale for the Info Age.

Reengineering Management: The Mandate for New Leadership by James Champy (HarperBusiness, \$13) reflects on the successes and failures of one of the decade's most influential management trends. Among its insights: "Genuine reengineering... has made much of the work of middle managers no longer relevant." Yipes! No wonder so many people have the downsizing blues.

It's enough to make you want to escape to a less complicated age. That's almost possible via Richard S. Tedlow's **New and Improved: The Story of Mass Marketing in America** (Harvard Business School, \$17.95), which covers the past hundred years. Concentrating on the wars between Coke and Pepsi, GM and Ford, A&P and its rivals, and Sears Roebuck and Montgomery Ward, Tedlow's own new and improved edition—the book was first published in 1990—can be read for its valuable marketing lessons ("inventory is the price a business pays for lack of information") or just as a fascinating window on days gone by.

Neil Baldwin's **Edison: Inventing the**

Century (Hyperion, \$14.95) is another blast from the past. Here is a glimpse of the thinking and system-building ingenuity of this "Napoleon of invention." Here, too, is a look at one of the world's great contrarians: a millionaire who railed against wealth, a publicity seeker who craved solitude, the inventor of the light bulb who refused to adopt alternating current.

Horse sense of a different sort was demonstrated by Calumet Farm, which, from the 1920s through the 1980s, produced eight Kentucky Derby winners and champions aplenty before being hobbled and ultimately felled by owner J. T. Lundy's extravagance and chicanery. The stable's engrossing story is described in Ann Hagedorn Auerbach's **Wild Ride: The Rise and Tragic Fall of Calumet Farm, Inc., America's Premier Racing Dynasty** (Holt, \$14.95). Here are the glory days of Whirlaway and Citation—and the ignominy of the 1992 auction that saw the farm and everything on it sold to a Brazilian bidder for \$12,000.

In **1939: The Lost World of the Fair** by David Gelertner (Avon, \$13.50), the reader is transported to the period between the Great Depression and World War II. Part tour of the 1939 New York

World's Fair and part fiction, the exceptional book is chockablock with details about who Americans were and how they became. And in its celebration of an optimistic age, it's as filled with life as a Cole Porter ballad. "What mattered," says one of Gelertner's characters, "was the luminous feeling you got that, come what may, the future had good things in store for you if you persevered."

A more disquieting look back comes from Robert S. McNamara's **In Retrospect: The Tragedy and Lessons of Vietnam** (Vintage, \$15). With this book, McNamara broke his 27-year public silence regarding the Southeast Asian war. Not everyone was pleased with the result, particularly since the former Defense Secretary seems still to view the war as a management problem. At the same time, in this self-critical effort, McNamara lays out all the complex reasons for the tragic Vietnam crusade—some of which had to do with halting the spread of communism in Asia.

In the 1990s, the U.S. has unleashed a new and more potent crusade against communism: rampant capitalism. In Ying Zha's **China Pop: How Soap Operas, Tabloids, and Bestsellers**

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forming a Culture (New Press, gives readers an engaging view of *sibuxiang*—"a bizarre, hybrid ani- neither horse nor donkey"—that is a today. It's a land where the Com- ist Party elite rule, but where they share the spotlight with the stars re fantastically successful TV soap *ning* or make room for titillating os and movie-star interviews in *China Culture Gazette*.

it's a country where onal freedom is ex- ling—"as long as don't engage in : political protest." domestic politics more your meat, profiles of the ing Presidential idates may catch eye. **On the** **Clinton Pres-**

cy by Elizabeth Drew chstone, \$14) focuses on telling first 18 months in office ie man from Hope. And what a : they were, Drew shows: disorga- d, uncertain, and sluggish. "We e just reeling, we were just reel- Communications Director Mark D. an admits to Drew. In a new af- ord, the author considers how, since 1994 Republican landslide, Clin-

ton has been paying for his blunders.

Richard Ben Cramer's **Bob Dole** (Vin- tage, \$11)—excerpted from the author's 1992 tome, *What It Takes*—is un- abashedly positive toward its subject. Dole comes off as persistent, shrewd, even heroic. Fans and nonfans alike will be drawn in by Cramer's stories of Dole's hardscrabble Midwestern youth, war experiences, and evolution from GOP neophyte to hatchet man to key Washington power broker.

closing half the law schools to cut the number of lawyer-lobbyists. Too much? Some "60% of Americans see the coun- try on the wrong track, while half say Congress might just as well be chosen from voter lists or telephone directo- ries," he observes.

If the political heat is getting to you, perhaps you could use a chill. **The Com- ing Plague: Newly Emerging Diseases in a World out of Balance** by Laurie Garrett (Penguin, \$14.95) will give you plenty—750 pages on how such epi-



This season's bounty ranges from second thoughts on the Internet to McNamara's Vietnam *mea culpa*

However, if the whole Washington scene suggests images of a fetid swamp in- fested by special-interest parasites, maybe Kevin Phillips' **Arrogant Capital** (Back Bay Books, \$12.95) will suit you better. To free the political system from high-powered operators represent- ing narrow causes, Phillips proposes moving the capital to other cities for part of each year, replacing congression- al votes with national referendums, and

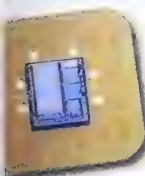
demics as AIDS, Ebola, Legionnaires' dis- ease, and malaria emerged and how the battle against them is going. Observes Garrett: "While the human race battles itself, fighting over ever more crowded turf and scarcer resources, the advan- tage moves to the microbes' court."

Right. Speaking of which, anyone for tennis?

BY HARDY GREEN

Green is BUSINESS WEEK's Books editor.

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BY STEPHEN H. WILDSTROM

A PHOTO LAB IN YOUR PC?

New scanners and printers will make it easier to produce high-quality images

Recently, I flunked an interesting test. Antonio Perez, general manager of Hewlett-Packard Co.'s Inkjet Products Group, showed me several prints of a snapshot. One was a conventional photographic print. The others had been produced on various computer printers, including some experimental models designed for home use. I couldn't figure out which one was the conventional print.

True, the test was a bit rigged because all of the pictures were covered with plastic, making it hard to examine the surfaces closely. But the demonstration left me convinced that PCs are the future of amateur photography.

Although digital cameras are carving out a healthy niche for themselves, the overwhelming majority of pictures will continue to be taken on film, which offers a so-far unbeatable combination of price and quality. The trick is getting digital versions of your conventional photographs into your computer and getting the "prints" back out.

This is getting a lot easier. Some models of HP's Pavilion home computers have built-in scanners that can handle a snapshot. For \$400 to \$600, you can get color scanners such as the HP ScanJet 4P, the Umax Vista-S6E, and the

Apple OneTouch—and prices are dropping fast. Some offer accessories that will scan a 35mm transparency. And HP is developing a scanner that will even create a digital image directly from a color negative.

If you have a video camera, there's another low-cost way to get professional-quality images. The \$200 Snappy from Play Inc. will transfer a frame from any source—including a camcorder, tape, or



broadcast—into a Windows computer through a printer port.

Of course, once pictures are inside your computer, you can look at them on your screen, but most folks prefer their photos in albums or frames. Today, a \$300 inkjet printer can produce decent color images. The secret to getting the best quality is to use specially coated papers that prevent the ink dots from spreading out and blurring as they do on ordinary

paper. You can get more vivid colors and sharper output by using glossy paper specifically designed for high-quality inkjet printers. You'll want to use these papers only for the final "keeper" print because they can cost \$1 or more per 8½-by-11-in. sheet, but the result is a print that looks and feels like a lab-developed photograph. For snapshot-size pictures, Eastman Kodak Co. sells 4-by-6-in. photo-inkjet paper for \$10 for a pack of 36 sheets. Like all color prints, light exposure will cause fading over time, but manufacturers say they should be as stable as conventional photographs.

TIGHTER FOCUS. Over the next year or so, printers may get dramatically better at turning out photos. It will be years before color laser printers become cheap enough for most people, so inkjets will be the main attraction. Today's inkjets are currently designed by industry leaders HP and Canon Inc. for the best quality text, since that's what people care most about. But now, manufacturers are turning to the difficult job of accurately generating the millions of colors needed for faithful photographic reproduction.

HP, for example, is considering a line of photographic printers. With prices plunging, the company thinks consumers may be willing to buy one printer mainly for text and shell out an additional \$250 or \$300 for a separate machine just for photo-quality prints. The initial market would probably be amateur photographers, who are legendary for spending freely on new gadgets.

As professionals have known for years, computers are marvelous tools for manipulating photo images. What amateurs have lacked is a way to get the pictures into and out of a PC. That problem, it appears, will soon be solved.

BULLETIN BOARD

HARDWARE

SAVE THAT DATA

Summer is upon us, and that means thunderstorms, brownouts, and other electrical disruptions that can be hard on your computer and dangerous to your data. A new generation of compact, low-cost uninterruptible power supplies can help protect against voltage spikes or



sags and provide time for an orderly shutdown if the power goes out. The \$200 UPstart from S. L. Waber (800 634-1485) sits under your monitor with controls up front to turn your computer and peripherals on and off. If you run Windows, included software can save your configuration to disk automatically so you can resume where you left off when the power comes back. The device will also protect your modem from voltage spikes on phone lines.

SOFTWARE

APPLE POLISHING

Macintosh owners waiting for Copland, the long-delayed overhaul of the Mac operating system, may get a small break. Apple Computer Inc. now plans to release one last upgrade to its 5-year-old System 7 late this year. The new version, code-named Harmony, will integrate an assortment of bits and pieces that Apple has released, including improved networking and Internet tools, as well as some Copland features. Copland, the first version of Mac OS designed specifically for the PowerPC chip, isn't slated to ship until late '97.

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BY RUDI DORNBUSCH

WHY BAILOUTS ARE BAD MEDICINE



THE CURE:
Investors
should pay
when a nation
defaults. That
would force
the global
financial
system to
police itself
better

Financial authorities around the world are edgy. Hardly a month passes without the discovery of a major fraud—Metallgesellschaft, Barings, Daiwa Securities, Sumitomo Bank, and countless others. From time to time, an entire country goes over the financial cliff. Policymakers hope that new controls, regulations, and surveillance will soon be in place before some new disaster undermines the whole global financial system.

Until then, it's up to the market to punish transgressors. The disintegration of Barings and the vigorous prosecution of Daiwa in New York are cases in point. But punishment is much harder when entire economies are financially mismanaged.

Take the postmortem on Mexico's crash and rescue. The consensus view is that the crisis showed the need for two things: better surveillance and greater financial resources. But a third—no automatic bailout for investors—could be even more important.

Individual countries have the capability of regulating and supervising their own markets. If these jobs are performed conscientiously, large-scale accidents are less likely to happen.

But in the international community, it doesn't work that way. There is no internationally recognized body to establish rules for conduct on exchange rates or other macroeconomic management. If a country decides, for example, to secretly boost its money supply, no one is likely to challenge the policy. As long as foreign money continues to pour in, the Finance Minister rides high. By the time foreign investors discover the problem and money starts to dry up, it's too late to prevent a crisis. Then, when the International Monetary Fund and central banks try to help, the country is already deeply in trouble.

NO LACK OF DATA. We should not kid ourselves into believing that better availability of data would prevent this kind of crisis. There is plenty of information on growth, banking problems, interest rates, and trade. More data won't help investors who refuse to look at the facts.

In the Mexico rescue, the U.S. Treasury and the International Monetary Fund got together to arrange a colossal loan. Europeans in the IMF were railroaded into participating. The German position was that bailing

out investors is a mistake. The Bundesbank in particular believes that bailouts give investors a false sense of security and should be reserved for problems that threaten the entire financial system.

The U.S. view, by contrast, is that the global financial system is highly fragile. The Mexican crisis shows the risk of not having lots of money on hand for speedy intervention. The Clinton Administration had to beg the Congress for money even as Mexico teetered in meltdown.

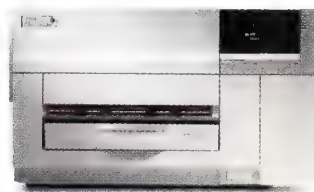
Both views of the bailout problem are, of course, correct. There is a hazard in telling investors that they will always be rescued. But there also is a risk if a country gets out of hand and threatens the entire global financial system. The question is how to strike a balance. In the 19th century, until the early 1980s, governments stayed away from bailing out private investors. The history of foreign lending is replete with distressed countries, defaulted loans, disappointed investors. Foreign Bond Holders Protective Councils organized the multitude of creditors and renegotiated the terms of agreements with defaulting countries. The councils worked pretty well. The U.S. council lasted till the mid-1960s.

CONFUSING SIGNALS. Nothing in the history of foreign lending suggests that the private market cannot handle credit or that country defaults inevitably become systemic crises. It is important to allow markets to work again and get governments out of the bailout business. Private investors have to learn about risk again and pass on their skepticism about bad policies to would-be borrowers. In such a system, good policies get rewarded by low interest rates and plenty of credit; bad policies bring about high penalties and a dearth of credit. The current system of presumptive bailout—based on the assumption that countries are too big to fail—confuses market signals, leads to bad policies, and, thus, creates recurrent problems.

So the next time a country goes into distress, international financial institutions and the major powers should turn their backs. That will demand ice water in the veins of international policymakers, but the world will go on, as it has for 150 years of country defaults. Teaching a lesson on a smaller scale frees up the financial system to intervene with great vigor when there is a real crisis.

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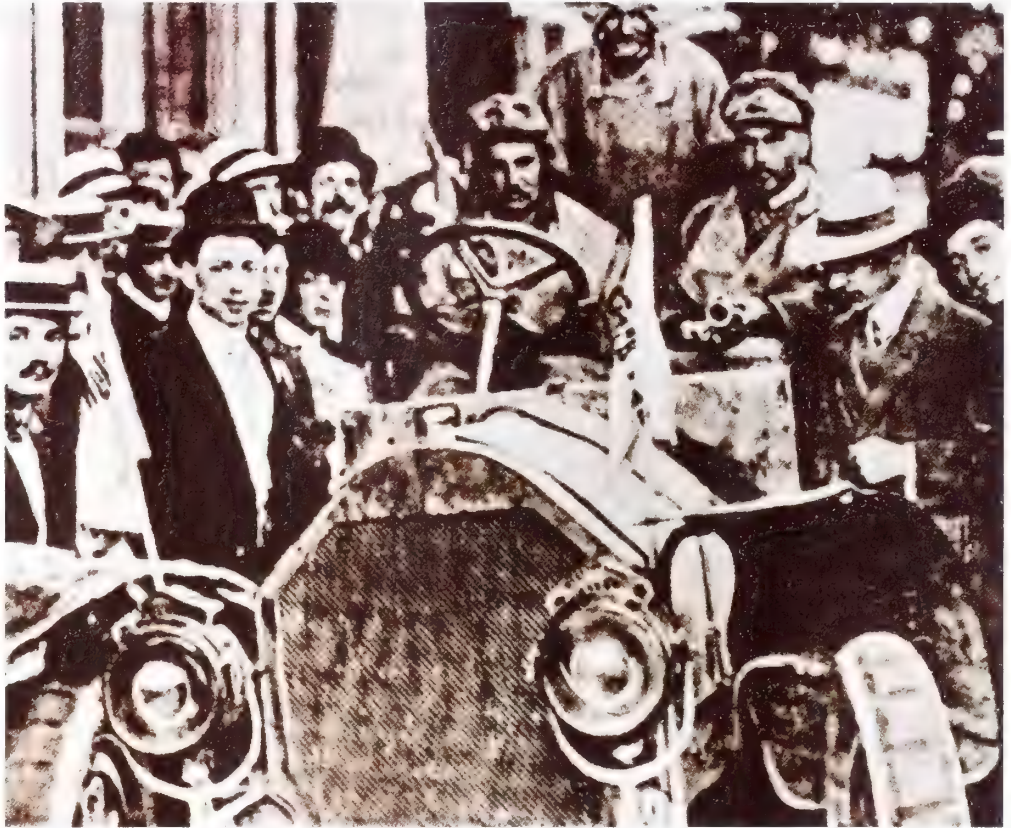


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BY GENE KORETZ

U.S. CURRENCY GROWTH EBBS...

It may signal less turmoil overseas

In case you haven't noticed, something strange is happening to the most tangible component of the money supply—the good old American greenback. After posting healthy gains in the early 1990s and indeed, during most of the postwar period, growth of currency in circulation slowed sharply last year. It is now expanding at its slowest year-to-year pace in more than 30 years.

"It's a mystery," says economist David H. Resler of Nomura Securities International Inc. "It's uncertain whether the slowdown in demand for paper currency is telling us something about foreign economies, the U.S. economy, or perhaps both."

THE BIG SLOWDOWN IN DEMAND FOR GREENBACKS



Resler notes that more and more greenbacks are exported—legally or covertly. Dollars are used for transactions not only in Panama and Liberia, say, which have adopted the dollar as their official currency, but also in Latin America, Eastern Europe, and the Middle and Far East.

Indeed, economists Richard D. Porter and Ruth A. Judson of the Federal Reserve Board estimate that as much as 70% of U.S. cash in private hands (currently about \$375 billion) may be held outside the U.S. More important, they say, some 80% of all currency growth since 1980 seems to be tied to rising foreign demand.

The big impetus behind such demand, of course, has been political and economic turmoil overseas, such as the breakup of the Soviet empire and the economic crises enveloping Latin America a few years ago. In fact, many experts attributed the slump in currency

growth last year to unfounded Russian fears that American plans to issue a new counterfeit-resistant \$100 bill would somehow affect the value of old banknotes. Thus, when the new U.S. C-note was finally issued this March, the betting was that demand for banknotes would start to accelerate again.

The fact that demand for U.S. currency has continued to languish—at least thus far—suggests an intriguing thesis to economist John B. Carlson of the Federal Reserve Bank of Cleveland. More and more, he observes, growth in U.S. currency seems to have become an index of international political and economic instability.

If that's true, he says, "the current slowdown in demand for U.S. banknotes may be signaling the recent success of economic and political reforms in Eastern Europe and Latin America."

...AND EXPERTS AREN'T SURE WHY

Some see a cashless society

Economic and political progress overseas may be contributing to the sluggish growth of U.S. currency, but economists think domestic developments are also responsible. Lacy H. Hunt of HSBC Markets Inc., for example, points out that nominal gross domestic product—which reflects real growth plus price increases—has risen only 3.6% in the past four quarters, a historically low pace.

"The continuing absence of price pressures implies that people need to carry less cash to buy things," he says. "In part, slow currency growth simply reflects low inflation."

Economist William V. Sullivan of Dean Witter Reynolds Inc. believes that the escalating use of credit cards is gradually affecting the demand for currency. We may not yet be a cashless society, he says, but the growing use of plastic for such mundane purchases as movie tickets and groceries is an undeniable trend.

The upshot of such developments at home and abroad is that it is becoming increasingly difficult to decipher the implications of changes in currency demand—particularly since such changes have traditionally been correlated with shifts in retail sales.

"Currency growth may be telling us less about the economy's direction than it used to," muses Nomura's Resler. "But it's still telling us something."

'NO SMOKING' IS WORKING

Bans really make puffers cut down

Stroll by a Manhattan office building any weekday, and you're likely to see a band of loyal smokers who come outside for a cigarette. So how do workplace bans really reduce smoking very much?

Yes, report University of Maryland economists William N. Evans, Matthew C. Farrelly, and Edward Montgomery. Using survey data, they estimate that between 1985 and 1993, the portion of U.S. workers employed in workplaces that enforced smoking bans rose from 25% to 70%. As a result, they say, smoking rates among workers affected by bans fell 5 percentage points—that is, 5% more would have been smoking in 1993 without the bans. And those who maintained the habit would be smoking 10% fewer cigarettes a day.

BLAME IT ON HONG KONG

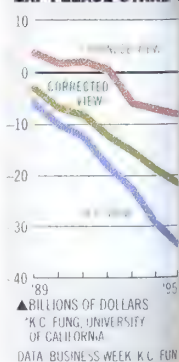
The gap in U.S.-China trade tallies

A source of tension between the U.S. and China is the wide gap between the two countries' estimates of America's trade deficit with China. According to Washington, it was \$33.8 billion in 1995. Beijing says it was only \$8.6 billion.

Why the difference? Among other things, China doesn't count its goods that are reexported to the U.S. from Hong Kong. And the U.S. doesn't count its exports to Hong Kong that wind up in China. Counting both sorts of re-exports and subtracting the markup added by Hong Kong middlemen, economist K.C. Fung of the University of California at Santa Cruz estimates that America's actual deficit has been about 35% smaller than the official U.S. version (chart).

Such adjustments presumably won't be needed after next year. That's when Hong Kong—and all its trade activities—will revert to Chinese control.

WILL THE REAL TRADE GAP PLEASE STAND UP?



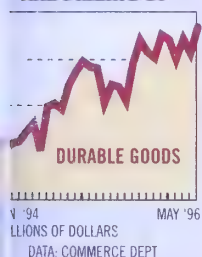
JAMES C. COOPER & KATHLEEN MADIGAN

N APPETITE FOR IMPORTS S GUTTING THE GOOD NEWS ON TRADE

U.S. ECONOMY Foreign trade was expected to add handsomely to the economy this year. Stronger world growth was supposed to raise exports while import growth slowed because of slacker domestic demand.

Now, trade improvement is not a sure bet. Exports still set to show more muscle. And increased foreign demand will help the turnaround beginning to bubble in the manufacturing sector. But imports will grow as well, lifted by surprisingly resilient demand in U.S. and by inventory rebuilding. As a result, foreign trade probably will not add much to this year's growth in real gross domestic product.

FACTORY ORDER BOOKS ARE FILLING UP



ly. In anticipation of Lyons, Canadian and European leaders already have expressed frustration with U.S. trade policies.

The talks are unlikely to yield any major policy results, but the forum should be a pre-election bonanza for President Bill Clinton, who gets to brag about his chief economic point, the economy. Although economists tend to give the Federal Reserve more credit for the economy's recovery than they give the White House, the U.S. nevertheless brings to the summit the best mix of growth, inflation, unemployment, and deficit reduction among the G-7.

LATEST EVIDENCE OF STRENGTH comes from U.S. manufacturers. In another sign that the factory sector is gaining momentum, orders for durable goods jumped 3.3% in May, double economists' expectations (chart). Orders so far in the quarter are well above the first-quarter average.

Aircraft orders, which can be volatile from month to month, accounted for the lion's share of the May rise. Including transportation, bookings increased only 0.7%, that was the fifth increase in the past six months. Orders through May have turned up strongly after a lackluster first-quarter showing.

The Commerce Dept. does not break out foreign and domestic orders, but the May report from the nation's purchasing managers showed a big rebound in export orders, suggesting that foreign demand is an important component in the recent factory strength.

Even so, the U.S. trade balance is looking like less of an asset for future U.S. growth, getting off to a poor start in the second quarter. The deficit of goods and services slipped in April, to \$8.6 billion, from \$8 billion in March. After adjusting for prices, the April deficit is greater than the first-quarter average.

EXPORTS OF GOODS AND SERVICES rose 1% in April, to \$69.9 billion, but imports advanced by a stronger 1.7%, to a record \$78.6 billion. Oil imports jumped 31.3% as a \$2 per barrel rise in crude prices added to the U.S. energy bill. So far this year, merchandise exports and imports are growing slower than they were a year ago (chart), but both downtrends are set to reverse soon.

Merchandise exports have tapered off across most regions, except for those bound for Japan and Mexico. Of course, stronger Mexican demand is mainly a bounce-back from last year's recession, when its imports collapsed. Still, the Mexican economy has picked up faster than some expected. So Mexico's purchases of U.S. goods will strengthen over the rest of the year.

The 12.1% increase in goods exports to Japan can be traced partly to the past weakness of the dollar vs. the yen. But U.S. exporters will get little help from the dollar in coming months, since it has already appreciated 30% against the yen since the spring of 1995. On the plus side, though, Japan's burst of economic activity in the first quarter, when growth surged at an annual rate of 12.7%—a 23-year high—signals that its recovery is firmly in place.

U.S. manufacturers should also get a lift from the European recovery. Europe's upturn is unlikely to be strong, however, mainly because of public spending cuts as governments struggle to meet the Maastricht Treaty criteria for a single-currency Europe. By 1997, public deficits must fall to 3% of GDP.

Nevertheless, Germany is emerging from its recent slump, while Britain is picking up steam, and Spain's

FOREIGN TRADE IS SET TO REBOUND



Business Outlook

outlook is improving. France and Italy are laggards, but a modest upturn in Germany should pull the rest of Europe along, providing support for U.S. exporters.

Prospects for improvement in the U.S. trade deficit would look impressive if exports were the only factor. The problem is that imports could very well take off as well because of the staying power of demand so far this year and some inventory rebuilding this summer.

Inventories have barely kept up with the unexpected gain in sales. The ratio of business inventories to sales fell to 1.38 in April, the lowest ratio in more than a year. As manufacturers and retailers restock shelves, they will increase ordering from foreign producers as well as American manufacturers.

On the positive side, imports should hold down inflation. Import prices in May, excluding petroleum, have fallen 0.8% from a year ago, compared to non-energy consumer inflation of 2.7%. The recent strengthening of the dollar should continue that trend.

AS LONG AS CONSUMERS keep spending, though, imports will flow in, worsening the trade deficit. For now, shoppers show few signs of a pullback. Despite higher mortgage rates, sales of existing homes, which account for 85% of all single-family-home demand, increased in May, to an annual rate of 4.26 million. That matches a record high hit nearly three years ago.

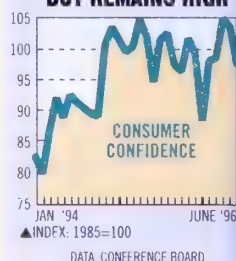
And despite a drop in June, the level of consumer

confidence remains high. The Conference Board's index dipped to 97.6 from 103.5 in May (chart). A sharp drop in consumers' assessments of present conditions accounted for much of the fall. That component fell nine points, to 111.4 in June, but the Board says that's still a "high reading" by historical standards.

The Conference Board's confidence index remains close to its average during the past year and well above its 1994 level, a year in which consumer spending grew a sturdy 3%. Moreover, while the board's numbers zigged downward in June, the widely followed index of consumer sentiment compiled by the University of Michigan zagged steeply upward in the same month.

The key to this year's contribution from trade will hinge on how strongly import growth picks up. Imports continue to grab an ever-greater share of domestic demand, in large part because of the boom in high-tech investment. Although overall capital spending is slowing down, that sector of capital-goods demand continues to grow strongly. Add in a surprisingly sturdy consumer sector, and import growth seems set to nullify what shaping up to be a good year for U.S. exports.

JUNE CONFIDENCE DIPS BUT REMAINS HIGH



GERMANY

GERMANY INCHES TOWARD HEALTH

Germany's mini-recession, in which real gross domestic product fell in both the fourth and first quarters, is now over. Growth is rebounding in the second quarter, but the recovery in the second half—and into 1997—will be moderate at best as structural problems keep joblessness uncomfortably high.

The harsh winter and its jolt to construction, which was already in a post-unification slump, exaggerated the economy's weakness. In April, milder weather sent construction output roaring back, helping to push industrial production well above its first-quarter level.

But it's not just construction. Manufacturers' orders—domestic

and foreign—are strengthening. Business confidence rose in April and May, the first two-month gain since late 1994 (chart). Domestic demand is buoyed by low interest rates and tax cuts for low-income

families. Real incomes are rising as wage gains manage to outpace inflation of only 1.2% in June. Auto sales are strong, and retailers' confidence is rising. Foreign demand is responding to the 6% drop in the trade-weighted value of the mark from its

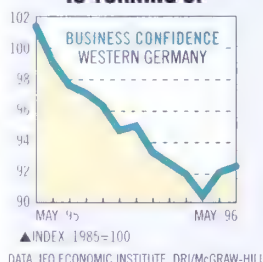
all-time high in March, 1995.

Germany's cyclical and long-term problems, however, will limit growth. In the near term, excessive inventories will remain a drag on manufacturing, though better

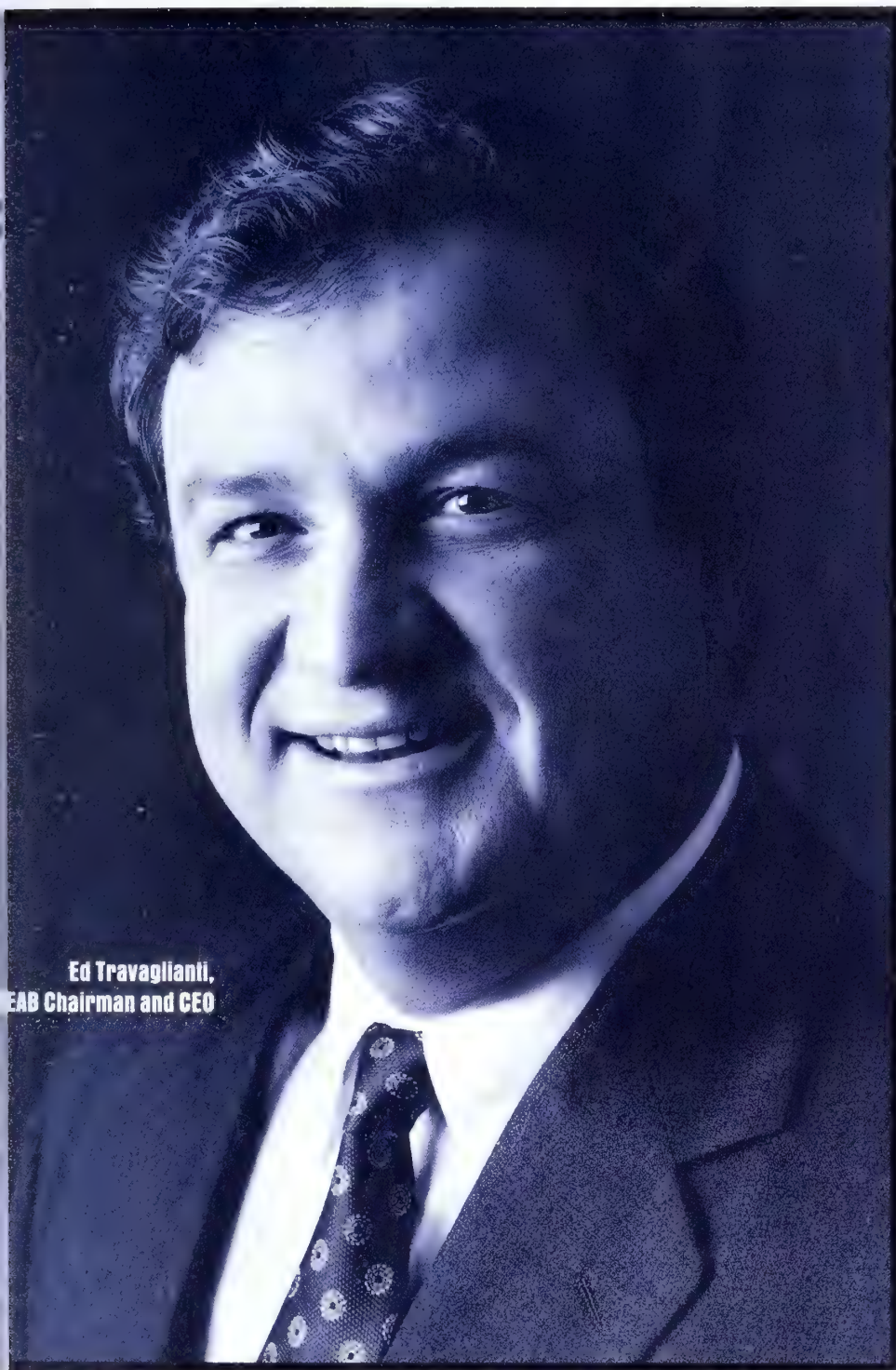
demand should clear away the excess this summer. Equipment investment has been soft for a year, but the demand pickup, along with the lower mark, interest rates, and labor costs, will help. After its spring rebound, construction will weaken in the second half.

The real obstacles, though, are structural, with joblessness heading the list. Unemployment fell in May, but only in the East, where winter weather was rough. May's 10.3% jobless rate, near a post-World War II high, is unlikely to fall by much this year, given the modest growth outlook. The Bundesbank recently endorsed a government package of tax and spending cuts aimed at deficit reduction, deregulation, increased competitiveness, and, ultimately, lower unemployment, but opposition to the proposals is broad and intense.

FAITH IN THE FUTURE IS TURNING UP



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Ed Travaglini,
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GOING FROM THRILL

Microchip makers can't fool themselves any longer. Their notoriously cyclical \$144 billion industry has plunged into the sort of worldwide slowdown that was supposed to be obsolete. In recent weeks, the bad news has been pouring in from chipmakers around the globe: Lower profits. Production cutbacks. Layoffs. In the end, 1996 could be the industry's worst year this decade.

Nearly every major semiconductor maker is feeling the heat: On June 20, California's National Semiconductor Corp. said it will take a charge of some \$300 million in the quarter ending Aug. 25 to cover restructuring. Advanced Micro Devices Inc., Cypress Semiconductor Corp., and others say their earnings are being pounded, too. In Europe, shares of giant Philips are in a swoon over chip fears. In Japan, Fujitsu Ltd., Hitachi Ltd., and others are scaling back huge planned expansions in production. From South Korea to Taiwan to Idaho, other chipmakers are also being rocked.

The critical questions for the chip industry and the investors who have bet heavily on its fortunes: Just how bad is it going to get? And how long can this devilish downturn last? One of the more pessimistic market watchers, Pathfinder Research Inc. in San Jose, Calif., forecasts a 9% drop in total semiconductor revenues in 1996—a gut-wrenching decline after last year's 42% gain. And Pathfinder's outlook for dynamic random-access memory (DRAM) chips is much gloomier: a plunge of 36%. Faced with a possible glut, DRAM producers are scrambling to trim output. "We can't

get around the fact that the DRAM business is a commodity market," says Thomas J. Engibous, president of Texas Instruments Inc.

Many market watchers aren't as pessimistic as Pathfinder. But any slowdown at all makes a mockery of what market gurus and chipmakers had been proclaiming: the end of their industry's cyclicality. Eternal double-digit growth was almost assured, they said, because chips have become so pervasive—vital components in everything from cars to computers to consumer electronics.

Bushwa. Richard L. Whittington, an analyst with SoundView Financial Group, proclaims that "1996 is a washout." Already, investors are feeling the pain. Hammered since late last year, chip stocks are now really getting whacked. Cyrix Corp. dropped 26% after warning on June 20 of a likely loss this quarter. The Philadelphia Stock Exchange's Semiconductor Index has lost 41% since its high-water mark, posted last September. "The downturn seems to be affecting just about everybody," says Robert K. Beachler, strategic marketing

director at chipmaker Altera Corp.

More bad news may be in the offing. The Semiconductor Industry Association's book-to-bill ratio, which tracks the backlog of customer orders for chips against U.S. factory shipments, reached its lowest point ever in April, when it hit 0.79 (chart). It had been at an all-time high of 1.19 just eight months earlier.

SELF-INFLICTED. Still, none of this means the high-tech sector is heading for a tank. Unlike previous chip crises, this one wasn't triggered by a huge drop in demand. Rather, chipmakers inflicted pain on themselves. After five years of increasing new capacity cautiously, they added new factories *en masse* last year. By the fourth quarter, 48 new plants were spewing out chips for a hollow boom that fell short of expectations.

Continued growth in demand will spare some companies. PC sales are projected to climb 19% worldwide this year, according to market researcher International Dataquest Inc., down a bit from last year's 25.6%. PCs remain the gravy train for chip suppliers, accounting for about 10%

AROUND THE GLOBE, SIGN



ADVANCED MICRO DEVICES will report an unspecified loss in the second quarter, mainly because of declining sales of its important memory products.

CYPRESS SEMICONDUCTOR will delay by six months the construction of a fifth chipmaking plant because of slipping profits.



CHILLS

Suddenly, the chip biz is plunging. How bad will it get?

sales. That is makers of microprocessors, complex logic chips, and other proprietary products will ride through the downturn. One of the unscathed—so far—is giant Intel Corp. It expects to notch a second quarter that equals its first quarter when it earned \$894 million on sales of \$1.6 billion. And Intel says its gross margins should hold strong, at around 35%. Other makers of high-margin, specialized chips—such as S3, Xilinx, Analog Devices, and Microchip Technology—will be on the upswing by the end of the third quarter, predicts Prudential Securities analyst Mark Edelstone. The real squeeze is being felt by the Three makers of DRAMS—Korea's

Samsung and Japan's NEC and Hitachi. Prices on the spot market are in free fall, declining 75% since November. As a result, earnings of Asian chipmakers could plummet 40% to 50% this year. America's DRAM specialist, Micron Technology Inc., might fare even worse. Its second-quarter earnings were off 74% from a year ago, falling to just \$58 million on sales of \$771 million.

PIPE DREAMS. There are ominous signs that the price crunch is spreading. DRAM suppliers are switching production to more profitable designs, such as logic chips. Now, some of these markets are

getting overcrowded, pinching more U.S. companies, including Cypress and Lattice Semiconductor Corp. Even Motorola Inc. has delayed two plant expansions.

Hard to believe, but this downward spiral was touched off by a minor shortfall in holiday PC sales. The industry was looking for a 40% surge, not the 25% one it got. That left PC makers and chip suppliers holding bags of DRAMS. But chipmakers kept on pumping out silicon, betting on a pickup in 1996. "Semiconductor manufacturers had very unrealistic expectations for growth in PCs," says Vladi Catto, Texas Instruments' chief economist.

The roots of the delusion trace back to Asia, circa 1989. Reacting to soft sales and a weak domestic economy, Japanese memory makers put the brakes on new plants. Instead, they ran existing factories at full tilt to squeeze out juicy profits. It worked: Memory chips stayed tight, prices held firm, and profits were enormous. But the strategy also enabled Korean rivals to grab more market share, since they were less adverse to plowing DRAM profits into new plants. Samsung Group climbed to the

SEMICONDUCTOR BOOM IS OVER

TECHNOLOGY temporarily closed a new plant in February. Earnings for the quarter ended May 30 were 6% compared with 1995.

SUBISHI, FUJITSU, HITACHI are going back somewhat from plans for increases in memory-chip production.

NATIONAL SEMICONDUCTOR will take a charge of about \$300 million in the quarter ending Aug. 25 to cover cost-cutting and revamping of its product line.

SAMSUNG will shut factories two days a month for the rest of the year to lower monthly output of 16-megabit memory chips to 12 million.

DATA: COMPANY REPORTS

top of the heap—and earned billions from DRAM chips.

Japan's restraint produced the longest period of sustained prosperity in semiconductor history. But with no end in sight, the Japanese joined the latest round of plant-building. Technology improvements added to the glut. The resulting surplus of memory capacity may last through much of 1997, warns Edel-

stone. A continuing worry: Chipmakers are slated to add another 49 fabrication plants in 1997, figures analyst George Burns of Strategic Marketing Associates in Santa Cruz, Calif.

The wild card now is whether Asian producers really will pare back planned production hikes. Some analysts suspect empty promises made as a ploy to boost the spot-market price of DRAMS. If so, a

glut could recur at any time. "It's like white-water rafting. All you can do is try not to hit the next rock," says Gary McDonald, a vice-president with memory supplier Kingston Technology Co. Easy to say. But not easy to do when business is in a downward spiral.

By Andy Reinhardt in San Mateo with Steven V. Brull in Tokyo and George McWilliams in Houston

CHIPS: THE FIGHT CLINTON CAN'T WIN

This is one trade fight a lot of Clintonites wish they had sidestepped. When executives in the semiconductor industry last year urged the Clinton Administration to press Japan to renew a bilateral chip accord, then-U.S. Trade Representative Mickey Kantor was all for it. The 1991 pact, which expires on July 31, was widely viewed in the U.S. as an exemplary agreement—albeit one with room for improvement. Besides, the Clintonites didn't want to say no to Silicon Valley CEOs whose support is vital to the President in California.

But now, the whole thing threatens to backfire on the Administration. On June 21, the two nations' chief negotiators, USTR Chief Counsel Ira Shapiro and tough-guy Vice-Minister of Trade Yoshihiro Sakamoto, ended talks without reaching a deal. One reason: Tokyo appears to be dead set against extending the accord. If Japan doesn't ease its opposition, the Administration will have to choose between walking away or settling for a nonbinding industry-to-industry pact. Either way, the Clintonites will look like losers. In a bid to avoid that fate, Clinton was expected to deliver a tough message to Prime Minister Ryutaro Hashimoto in Lyons, France, on June 27: It's time to stop stalling and start dealing.

NO SHOW OF GRATITUDE. The White House is dismayed that the President's amicable visit to Tokyo in April yielded no breakthroughs in disputes over chips—or film or insurance or landing rights for U.S. airlines, for that matter. "We thought



SAKAMOTO: MITI says chips aren't even on the table

we left Tokyo with a shared understanding that credibility about the alliance depended on progress on the economic side," gripes a White House official. Others complain that Hashimoto isn't showing any gratitude for the jump his approval ratings took in polls after Clinton's visit. Hashimoto "owes us," says one trade hand.

U.S. Ambassador to Japan Walter F. Mondale is fuming,

U.S. officials say, over his June 23 meeting with Sakamoto's boss, Shumpei Tsukahara, head of the International Trade & Industry Ministry (MITI). Tsukahara told Mondale that extending the semiconductor accord was a nonstarter and that Clinton shouldn't even raise the issue in talks with Hashimoto.

On the surface, it's hard to see why the U.S. is making such a fuss. Since the inception of the '91 agreement, the foreign share of Japan's semiconductor market has more than doubled, to 30% (chart)—well above the 20% target of the accord—with U.S. producers accounting for about two-thirds of that. A number of collaborations have sprung up between U.S. chipmakers and Japanese companies to tailor semiconductors for specific products. "There's no compelling need for an agreement anymore," says Michael Smith, who

negotiated the first U.S.-Japan chip accord in 1986.

But many American companies worry that without an ongoing obligation for both governments to monitor foreign sales, Japanese purchasers won't buck pressure from local suppliers to buy Japanese chips. "The fear is people will revert to their insular ways, and our market share will drop," says a U.S. high-tech executive.

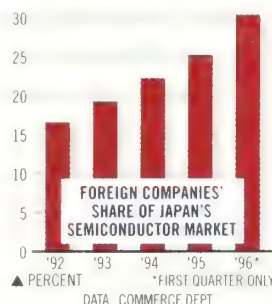
SMELLS A RAT. Whatever happens, any new accord will be far less stringent than the old one. The follow-up agreement Washington is pushing for contains no specific market-share target and no requirement that Tokyo lean on Japanese users to buy foreign chips. In a deft tactical move, MITI has lined up European support for an alternative: scrapping the accord and replacing it with some sort of multilateral forum.

The Japanese are wary of the U.S. proposal, especially its reference to "continued improvement in market access" as a goal. "It's a disguised attempt to lock in a 30% market share," says Stanton D. Anderson, a Washington lawyer who represents the Electronic Industries Association of Japan.

But Clinton, still seeking election support from Silicon Valley execs, shows no sign of backing down. Some U.S. officials concede it might have been wise just to let the Japan chips accord expire. Now, it's too late for that, and the U.S. is stuck in a spat it will find hard to get out of gracefully.

By Amy Borrus in Washington

CHIPS AHOY



THE UNLIKELY DOVE

Alan Greenspan is resisting interest-rate hike

When Federal Reserve Chairman Alan Greenspan was sworn in for his third term on June 25, it was with the dismay of a small band of liberal Democrats in the Senate who had led his confirmation for months. Under the inflation-phobic Fed chief, thundered Senator Tom Harkin (D-Iowa), "growth and the living standards of average Americans have been sacrificed at the altar of high interest rates."

Only Harkin knew what Fed insiders are saying about Greenspan these days. To colleagues on the rate-setting Federal Open Market Committee and Administration officials, he is the tight-money hawk populists love to assail. Indeed, compared with other policymakers, he's looking at the Fed the way a hawk looks at a dove, reluctant to boost rates to slow the economy.

In private conversations with Administration officials, private economists, colleagues, and others, the 70-year-old Greenspan expresses confidence that the second-quarter surge in economic activity—which may reach a 4% growth rate—will abate by late summer without need for tightening. That puts him at odds with several presidents of the 12 regional Federal Reserve banks who are worried that growth will remain strong enough to spark higher inflation. "Greenspan is at the end of the distribution and the presidents are at the other," says a former Fed official. "If we get a bad report, they would prod him to raise rates."

URGENT. Few Wall Street economists are bracing for a rate boost at the FOMC's July 2-3 meeting. But if the economic spurt continues into August, pressure will build on Greenspan to raise rates on Aug. 20, when the FOMC meets next. Still, the Fed chief is likely to resist if he sees no evidence of rising inflation. "I sense Alan feels no urgency to tighten," says David M. Hayes, chief economist for Aubrey G. Weston & Co., a securities firm.

Why is Greenspan so sanguine about inflation? For one thing, he doesn't believe that a spurt of strong growth and low unemployment are tinder for spark inflation. He's also counting on the percentage point jump in long-term interest rates since the beginning of the year

to dampen demand in coming months.

By contrast, the FOMC hawks share growing concerns about tightening labor markets, which are causing spot shortages and bidding wars for a number of workers. Some Fed bank presidents believe that the unemployment rate, which has hovered between 5.4% and 5.6%, is approaching the point at which price pressures should start building. In economic jargon, this is known as NAIRU—the nonaccelerating inflation rate of unemployment.

Since the FOMC's last meeting on May 21, the presidents of the Boston, Richmond, San Francisco, and St. Louis banks have warned that the tight labor markets, combined with continued robust growth, could lead to a run-up in prices. Richmond Bank chief J. Alfred Broadus Jr. frets that the jobless rate leaves a "lack of headroom," and Federal Reserve Bank of San Francisco President Robert T. Parry warned that inflation risks "may be somewhat on the high side."

But by Greenspan's reading of the tea leaves, the inflation threat remains low. Some of his favorite economic indicators, such as surveys of supplier deliveries, aren't showing the delays or bottlenecks that trigger higher prices. What's more, the Fed chairman is dubious about the predictive powers of NAIRU. Fixating on a single trigger point is risky, he

has said, since labor markets are local, not national.

Greenspan is also leery of firing a preemptive strike against wage hikes that is based solely on anecdotal reports of isolated labor shortages.

He's mindful that shortage scares have occurred repeatedly over the past 18 months



and have yet to trigger a broad rise in wages. But FOMC hawks may be reluctant to wait much longer for fear of falling behind the curve in their inflation battle. "If you're forward-looking,

you have to move on anecdotal data," says one regional bank official. "Relying on statistics is looking through a rearview mirror."

While Greenspan would deny it, some Fed watchers believe the chairman also has a political reason to keep the FOMC on the sidelines: After insisting to his congressional critics that the Fed fights inflation, not growth, he may feel compelled to prove that the central bank believes its own rhetoric. And he's likely to receive support for the status quo from President Clinton's latest appointees to the Fed:

Former White House Budget Chief Alice M. Rivlin, the new vice-chair, and Laurence H. Meyer, who had been running his own economics firm in St. Louis.

Fed watchers are laying odds that Rivlin and Meyer will be reluctant to kick off their terms by voting to raise interest rates.

But can Chairman Greenspan keep the increasingly restive regional bank presidents at bay? At his swearing-in ceremony, he jokingly thanked the economy for being so compliant in recent years. Now, he has to make sure that his FOMC colleagues will be just as cooperative.

By Dean Foust in Washington

DANGER ZONE





HARMONIZING: Lott (with mike) practices with the Singing Senators

CONGRESS

NEW SPARK PLUG FOR THE SENATE

Conservative Trent Lott is cutting deals as Majority Leader

'Gridlock" doesn't seem to be part of Trent Lott's vocabulary. In his first two weeks on the job, the Senate Majority Leader revived dormant health-insurance-reform legislation, pushed for a bipartisan welfare overhaul compromise, and pledged a vote on the stalled Democratic proposal to raise the minimum wage. He even cut a deal with a liberal Senator, Tom Harkin (D-Iowa), to secure the confirmation of Alan Greenspan to a third term as Federal Reserve Board chairman. Not bad for a deeply conservative Mississippian dismissed by critics as too ideological to build consensus.

Lott, who entered the Senate in 1989, says he's just trying to do the right thing. "It's in the best interest of the Senate to try to work together across philosophical and party boundaries," he says. But Capitol Hill insiders are starting to wonder: How long can Lott's hands-across-the-aisle approach last? It's not just that he faces

mounting resistance from unyielding Democrats and GOP hard-liners in the House and Senate. Lott's deft legislative maneuvering is starting to make Bob Dole's Presidential campaign aides squirm. They fear that his dealmaking—meant to help Hill Republicans win reelection this fall—will aid President Clinton by letting him take credit for tax cuts and welfare and health-insurance reforms that pass on his watch. Dole's Senate was more confrontational, but it left Clinton with far less to crow about.

That doesn't seem to concern Lott.

GRIDLOCK BUSTER

Examples of Trent Lott's newfound pragmatism:

GREENSPAN NOMINATION Lott reached an agreement with Senator Tom Harkin (D-Iowa) to end the stalling tactics that had prevented final confirmation of Alan Greenspan to a third term as Fed chief

HEALTH CARE Lott seems ready to cut a deal with the White House to win passage of a modest health-reform package to protect workers who change jobs or have preexisting medical conditions

MINIMUM WAGE Lott may agree to a bill increasing the minimum wage, as long as Democrats agree to business tax incentives

CAMPAIGN REFORM Lott held a vote on comprehensive campaign finance reform, though the measure failed to pass

though. A fiercely ambitious pol, he hopes to make his mark quickly. "He wants to get off to a good start by appearing able to work with the other side," said Senator Russell D. Feingold (D-Wis.). The leader won plaudits from Feingold and other Democrats on June 25, when he brought campaign-finance reform to the Senate floor. The measure failed, and appears to be dead for the rest of the year. By merely scheduling the vote though, Lott, a bass crooner with the GOP Singing Senator quartet, showed his willingness to build bridges to all factions.

TALKING TURKEY. The same spirit was evident in Lott's work on the 1997 budget. Despite opposition from some hard-right members of the House, where he served for 16 years, Lott worked with House Speaker Newt Gingrich (R-Ga.), an old friend, to craft a blueprint that satisfied Republicans of all stripes. And he offered to talk turkey with Democrats on raising the minimum wage from \$4.25 to \$5.15 an hour. Even Senate Minority Leader Thomas A. Daschle (D-S.D.), who accuses the GOP of pursuing an "extreme" agenda, praises Lott "new willingness to work with us."

The 55-year-old lawmaker's honeymoon may soon end, however. He could have big trouble trying to sell flexibility to firebrand House Republicans disdainful of the other chamber's more pragmatic instincts. "It's still the same Senate," scoffs freshman Representative Mark E. Souder (R-Ind.).

Then there's the Dole camp, which is more concerned about winning the Presidential election than seeing a Republican Congress chalk up legislative victories that might actually help President Clinton in the polls. Acknowledging those fears, Lott has agreed to def-

action on sweeping tax reductions in 1996 to deprive Clinton of a chance to sign an election-year tax cut, GOP sources say.

GOP rebellions and Presidential politics may soon plunge the Senate back into gridlock. But for now, the new leader is determined to get something done.

By Richard Dunham, with Ma Beth Regan and Howard Gleckman, Washington

By Howard Gleckman

PINOCCHIO FOR PRESIDENT

Remember President Clinton's drive to raise the minimum wage? Just a couple of months ago, Democrats in Congress vowed to boost it 90¢, to \$5.15, by the Fourth of July. And how about Bob Dole's efforts to repeal a 1993 gasoline-tax hike? Just before quitting the Senate, the then-Majority Leader thundered that rolling back the levy by 4.3¢ a gallon was critical to the fate of the economy.

Well, the minimum wage is still \$4.25 an hour. And the federal gas tax stands at 18.4¢ a gallon. Even though Senate leaders finally agreed on June 25 to vote on both bills later this summer, the odds of either becoming law remain long. Why? Republicans are still insisting on limitations on the minimum-wage hike that Democrats deem unacceptable. And Democrats will stall the fuel-tax rollback until they get a minimum-wage bill they like.

CHARADE. Are Clinton and Dole outraged at these latest examples of legislative gridlock? Hardly. In truth, the issues are playing out just about the way the two Presidential contenders want. Clinton is perfectly happy to see the minimum wage stalled in the Republican-controlled Congress. And the last thing Dole wants is for Congress to pass a gas-tax repeal that the President then gets to sign into law.

Clinton prefers pounding the GOP for failing to pass a pay hike to actually seeing low-wage workers get a raise. After all, if Clinton really wanted to boost the minimum wage, he would have acted in his first two years in office, when he Democrats controlled Congress. Instead, he stumbled on the idea only after the Republicans took over Capitol Hill. "From a purely political standpoint," says one Administration strategist, "we would rather have the issue."

It's the same with Dole and the gas tax. Not only did the Kansan support higher fuel levies throughout the Reagan and Bush Adminis-

trations, he never really turned up the legislative heat to get the rollback passed. When the Democrats offered to link the gas tax and minimum wage in a single bill, Dole torpedoed the deal by throwing in a third measure that would make it easier for companies to negotiate work rules outside of collective bargaining. Because the provision is anathema to pro-labor Democrats, it

ended of the year, or—a cynic might note—just beyond the November elections. Once, Republicans promised to roll back the gas-tax hike permanently. But their latest six-year budget resolution (a plan called "Bob Dole's budget" by the GOP leadership) omits any mention of the gas tax whatsoever.

"OPENING SHOT." For Dole, the point is that Clinton proposed the '93 gas-tax hike. And sending a symbolic message about the President as a tax-and-spend Democrat is much more important to him than knocking down the levy for a few months. Says Dole campaign manager Scott W. Reed: "It was the opening shot of this huge tax-reform/tax-cutting debate we're going to have in the fall."

This being Washington, both proposals may yet pass Congress. The wishes of the Presidential candidates aside, plenty of incumbent lawmakers really want to bring home some goodies in the weeks before the election. Most congressional Democrats are determined to raise the minimum wage. And Republicans desperately want to get the issue behind them. At the same time, GOP lawmakers would gladly support any tax cut, even one that lasts only a few months. But chances are that politicking will continue to keep either measure from ever becoming law. "The likelihood of Congress sending

the President anything he can sign is about zero," predicts one Republican lawmaker.

As the campaign heats up, both Dole and Clinton will be spewing an endless stream of promises—tax cuts, balanced budgets, anticrime initiatives, to name only a few. But the candidates shouldn't be surprised if voters don't believe them. After watching the debates over the gas tax and the minimum wage turn into a political charade, who would?

Gleckman follows economic trends from Washington.



Clinton doesn't really want to raise the minimum wage, and Dole doesn't really want to roll back the gas tax

derailed the whole package for months.

Then there was the matter of financing the tax cut, which would have cost about \$4 billion a year. For weeks, Dole refused to say how he would pay for it. Finally, he suggested auctioning off broadcast spectrum to raise cash. Trouble is, congressional Republicans have decided to give away that spectrum to television broadcasters, and no one has yet come up with substitute bucks. But even if Congress had approved a spectrum sale, it would have paid for a gas-tax cut only through the

CORPORATE ESPIONAGE

CLOAK AND DAGGER IN THE LAB

J&J is being charged with espionage by a medical-gear rival

Dozens of executives were meeting at an Indianapolis hotel in September, 1992, to discuss top-secret marketing plans and the relaunch of a crucial product. Unbeknownst to them, a sleuth from a bitter rival had slipped in. Quietly, he picked up documents and competitive data that days later would be turned over to his company.

A scene from the murky worlds of Tom Clancy or John Le Carré? The al-

mer industry exec recalls employees' being caught red-handed rummaging through a rival's dumpster. Indeed, Boehringer itself concedes, as J&J claims, it engaged in skulduggery on two occasions. At a 1992 convention, a Boehringer employee represented himself as a potential LifeScan customer to hear about a new product. And in April of this year, a sales rep picked up a LifeScan manual from a distributor's waiting

tion says the alleged spying was carried out by a small team within the marketing department and by outside consultants. Boehringer alleges higher-ups encouraged spying with the incentive of the cash awards named for famous sleuths: "Inspector Clouseau," "Columbo," and "Mrs. Fletcher." Several J&J executives acknowledge the awards but insist they were designed to reward legitimate information gathering.

ENOUGH DISCIPLINE. J&J was informed of Boehringer's allegations in August, 1993, by lawyers for the company, and launched its own investigation. Boehringer sought compensation from J&J ranging from the right to license a J&J product to straight cash, but discussions between the parties broke off in mid-June, 1994. The lawsuit followed.

A J&J spokesman says that sufficient

DIRTY TRICKS?

In a lawsuit filed in federal court in Indianapolis, Boehringer Mannheim alleges that Johnson & Johnson's LifeScan engaged in industrial espionage. J&J won't comment on specific allegations but says that employees engaged in some "improper activities." The charges:

SEPTEMBER, 1992 At a Boehringer sales meeting in Indianapolis, a LifeScan employee attends undercover and takes confidential documents and copies of a speech on the relaunch of a blood-monitoring device. The material is presented at a LifeScan meeting in early October.

FEBRUARY, 1993 At a Boehringer sales meeting in Orlando, a LifeScan employee attending undercover hears that the device, Accu-Chek Easy, is not selling well.

SEPTEMBER, 1993 At a Boehringer meeting in Istanbul, two LifeScan employees learn about a product under development and set in motion a plan to obtain a copy of the device and transfer it from Germany to LifeScan's California headquarters.

MARCH, 1994 A LifeScan consultant attends an Orlando sales meeting of Boehringer and takes 75 pages of confidential documents.

AUGUST, 1994 Boehringer alerts J&J to the suspicious activities and seeks a settlement.

JUNE, 1996 Discussions between Boehringer and J&J break down. Boehringer files suit.

DATA: COURT DOCUMENTS

leged derring-do is actually part of a sweeping set of industrial espionage charges filed in federal court on June 19 by Indianapolis' Boehringer Mannheim Corp. against LifeScan Inc., a Milpitas (Calif.) unit of Johnson & Johnson. The suit provides an extraordinary glimpse at how a battle for information on rivals can spin out of control.

Boehringer and LifeScan are fighting tooth and nail for leadership in the \$1.75 billion market for blood-monitoring devices for diabetics. Each has a 40% market share now. The suit alleges that senior employees of LifeScan "deliberately fostered an environment which made clandestine and illegal activities both routine and expected." J&J will not comment on specific allegations but admits it engaged in some "improper activities."

Intelligence-gathering among medical-equipment makers, say several longtime industry observers, is not new. One for-

room. It was eventually returned to J&J.

Still, nothing the industry executives have seen can match the alleged dirty tricks undertaken at LifeScan—a series of actions J&J Chairman and CEO Ralph S. Larsen now says "was not only incredibly wrong. It was incredibly stupid and will not be tolerated." Boehringer alleges, for example, that at a two-day company sales meeting in 1993, a LifeScan marketing employee who has since left the company, Noureddine Akli, "eavesdropped" on the proceedings. The information he uncovered—that a device, Accu-Easy, was not selling well—was allegedly given to Akli's boss, Daphne Flamer, and turned over to the LifeScan sales force.

One source familiar with the opera-

disciplinary action has been taken against offending employees and that steps have been taken to ensure that events do not recur. The company insists that none of its senior management was aware of the activities, and Larsen has criticized the events to managers J&J units worldwide. Three former employees named in the suit have left the company, the spokesman says, but he refuses to say under what circumstances. One, Flamer, did not return calls. Another, Wei Huang, could not be reached. David Van Avermaete, still with the company and the most senior executive named, referred calls to a spokesman who declined to comment on individuals.

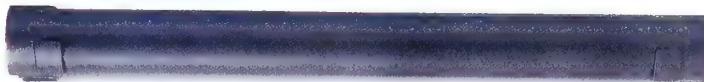
Still, the suit's allegations are numerous—and serious. Checking them could keep both Inspector Clouseau and Columbo plenty busy.

By Richard A. Melcher in Chicago and Joseph Weber in Philadelphia



monday configure 1

Full-Function Notebook
Lithium Ion Battery
Internal Diskette Drive



Detachable
lithium ion
battery
also
functions
as a
handle
and a
keyboard
tilt.

Choice of SVGA
displays from
11.3" CSTN
to 11.8" TFT.



Programmable keys provide
one-touch access to mobile
applications.

Up to 133 MHz
Pentium[®] processor,
hard drives up to 1 GB.

I want a notebook that's as flexible as I am. I want it to be full function with a long-lasting battery.



COMPAQ



FOLLOW-UPS

DAY OF RECKONING AT ASTRA

Bildman, accused of sexual harassment, and three others are out

Most companies try to sweep scandal under the carpet. Not Astra, the giant Swedish drugmaker. Confronted by allegations in a May 13 BUSINESS WEEK cover story of widespread sexual harassment and other abuses at its Astra USA Inc. subsidiary, the company quickly suspended three top executives and launched an internal probe.

Just weeks later, on June 26, the parent company took decisive action: It announced that it had fired Astra USA President and CEO Lars Bildman without paying him any severance. Although Astra won't comment on specific sexual-harassment allegations, Carl-Gustav Johansson, an Astra executive vice-president, says the investigation found that Bildman had "exhibited inappropriate behavior at company functions" and had "abused his power." Another suspended executive, George Roadman, also was shown the door, while a third, Edward Aarons, resigned. A senior executive in Sweden, Anders Lönner, was asked to resign for failing to report the misconduct to superiors, Astra says.

Airing yet more dirty linen, Astra also disclosed that it believes Bildman used company funds to pay for about \$2 million worth of personal expenses during the past decade. The bulk of the money supposedly came in the form of renovations done on three Bildman houses by

Astra-paid contractors. Bildman allegedly also used company money to pay for lavish vacations and other personal expenses. The U.S. Attorney's office and Massachusetts Revenue Dept. officials have opened probes of the alleged misappropriation of funds, Astra says.

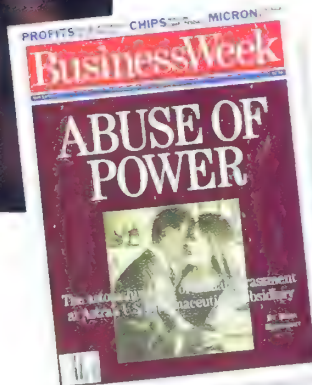
In a statement issued by his attorney, Bildman denied personal involvement in sexual harassment and "categorically denied" the allegations of financial improprieties. He also claimed to have canceled checks proving he paid for the renovations and called the decision to fire him a "cowardly and disloyal" action. Astra says Bildman did pay for some, though not all, of the renovations.

DISPUTED DOCUMENTS. To some degree, demonizing Bildman may serve to deflect blame from Astra itself. Many outsiders believe Bildman could not have run amok for most of his 15 years at the helm of the U.S. unit if he had been properly supervised by the parent company. Johansson hotly disputes that. Bildman was "expert at handling these things within the organization," so the parent company "had no chance" of finding out about the improprieties, he contends.

Indeed, in the weeks before the BUSINESS WEEK story was published, the Astra investigators say, Bildman was trying to hide information from the parent company. He hired a consultant, Lars Mag-

INVESTIGATOR JOHANSSON

Astra also alleges that Bildman used about \$2 million for personal expenses



nusson, allegedly to help with the cover-up. During at least two weekends, the investigators contend, the two men were seen shredding documents at headquarters. Magnusson, they say, allegedly spirited away documents that are now the subject of a legal battle between Astra and Bildman. Magnusson did not respond to requests for comment. Bildman's attorney denies a coverup or shredding of documents.

Bildman and Magnusson also allegedly conducted a secret campaign to discredit or deflect BUSINESS WEEK's story before it appeared. Two Astra

insiders say they were

asked by Magnusson and an executive to secretly tape phone conversations with BUSINESS WEEK. Both say they refused.

SECRET OFFICE. Bildman seemed to suspect that the article was being orchestrated by enemies within Astra, the investigators claim—an idea Bildman's lawyer calls "ridiculous." Whatever the reason, Bildman and Magnusson set up a secret office in a nondescript building not far from Astra USA's headquarters in Westborough, Mass. Staffed with computers and paralegals, the office apparently was intended "to be a nerve center for the effort to prove that BUSINESS WEEK was a tool of Astra USA's enemies," says Francis Carling, a New York lawyer who helped conduct the internal probe.

Is the misconduct at Astra USA really over? Several staffers say a recent national sales meeting was the quietest in memory, with limited alcohol and dancing. But some insiders contend a housecleaning should have gone much deeper. "The mentality is still there," says one female sales rep. "A lot of people who should still be looked at by [investigators] haven't changed. They're just quiet for the time being."

Maybe so. But experts say that Astra does any more housecleaning, it's likely to do so more discreetly over the next 6 to 12 months. Meanwhile, it already has done more than most companies in similar circumstances.

By Mark Maren
in Westborough, Mass.

tuesday
configure 2

Multimedia
CD-ROM
3 Lithium Ion Batteries
16 Bit Stereo Sound
Dual Speakers
NTSC/PAL TV Output



1
Batteries
Handle

2

Can run internal
diskette drive
simultaneously
with CD-ROM

3

Dual speakers
integrated into the
CD base provide
deep, crisp 16-bit
stereo sound

This base is
detachable
and houses the
CD-ROM

I want to use a CD-ROM with full-motion video. I want 3 batteries with up to 10 hours of life.



COMPAQ

By Greg Burns

THE FUTURES EXCHANGES HAVE LEARNED NOTHING

In March, amid the swaying royal palm trees at Florida's ritzy Boca Raton Resort & Club, leaders of some 50 global futures exchanges sat together at a giant U-shaped table, determined to show that they had learned a lesson from the 1995 disaster at Barings PLC. After all, if authorities in Japan and Singapore had compared notes on the activities of Barings trader Nick Leeson, he never would have racked up the \$1.4 billion in losses that eventually brought down the venerable British bank. To prevent another such debacle, the futures executives agreed to sign a sweeping information-sharing accord, each pledging to provide key data when the next trading crisis arose.

Now, though, in the wake of Sumitomo Corp.'s copper-trading fiasco, the deal struck under the Florida sunshine looks half-baked. Both the London Metal Exchange and the New York Mercantile Exchange signed the pact on Mar. 16. But the world's two competing copper exchanges haven't shared one whit of information about Sumitomo. The LME never answered

Nymex questions raised months before the crisis became public or shared data with the New York exchange after Sumitomo announced a \$1.8 billion loss in its London trading on June 13.

NO REPLY. On the morning after Sumitomo's bombshell, Nymex President R. Patrick Thompson arranged a conference call with LME Chief Executive David King to ask crucial questions: How would the Japanese bank unwind its positions? Would members of Nymex who also trade in London be put in financial jeopardy? What action should be taken—or avoided—in the U.S. to maintain an orderly market?

Thompson never got any answers,

and that left him to operate in the dark. Twice in three days, Nymex raised its margins—the downpayments required to trade—to curb volatility. But without communication from the LME, Nymex had no way to tell whether its margins were adequate. "We really didn't have any information. That's why we feel so frustrated," Thompson gripes.



COPPER FRENZY The hollowness of a recent global information-sharing accord was pointed up by the Sumitomo trading crisis

LME's King says his duty to protect Sumitomo's privacy kept him from sharing data about the firm with Nymex. Instead, he says, he shared what he knew with London regulators, who were in touch with the U.S. Commodity Futures Trading Commission. But Thompson says key information never reached Nymex.

The halting response to Sumitomo's loss illuminates crucial weaknesses in the exchanges' March pact. For one thing, since the exchanges are the first line of defense in a market emergency, they need information right away. As Thompson says: "If anything has to be done, we are the ones who have to do it." Yet the pact leaves direct,

market-to-market communication an option rather than a requirement.

Another problem: The exchanges' controls and monitoring procedures vary widely. For example, while the U.S. has strict rules requiring large traders to report positions daily, Britain does not. In practice, London exchanges collect such information by jawboning. The LME gathered "95%"

of the data it sought before Sumitomo announced its loss, King says. But he's mum on details, and critics doubt that the LME was keeping adequate tabs on the bank's trading. Says one U.S. official: "A lot of business flows to the LME at the expense of Nymex because they don't have a rigid system for monitoring trades."

NO EXCUSES. Exchanges still can't rely on their counterparts for the information needed to contain risk—pact or no pact. That sets the stage for more Barings, Sumitomos, or, worse, a crisis in which no deep-pocketed savior steps forward to cover the losses.

To make the exchanges' pact work, two key reforms are necessary. First, minimum global regulatory standards must be established. For example, every exchange should require that large traders post cash margins and report their positions daily. Exchanges should make it their business to know who is making big trades. Second, legal or regulatory barriers that discourage exchanges from sharing information with each other should be eliminated. There should be no excuse for cutting off direct communication.

No doubt, implementing such steps will be difficult. But without them, the pact that the futures folks signed in Boca Raton will be about as forceful as a tropical breeze.

Burns covers the futures markets for BUSINESS WEEK.

wednesday
configure 3

Slimline
51 Lbs
1.5" Thick



Memory expandable
up to 48 MB

Touchpad can be
replaced by an optional
trackball.

Internal diskette
drive is replaced
by a battery.

I travel light, real light. I don't need a floppy. And I want it all at around 5 lbs.



COMPAQ

SPORTS EQUIPMENT

A NEW VISION FOR ATHLETES

One Xcel's eye shields already have major-league backing

Two years ago, Ed Jarvis' 16-year-old son Ryan got poked in the face on his high school basketball court. The injury severed his optic nerve and blinded him in his right eye. A few months later, Ed allowed his son to resume playing basketball and football—provided he wear special shields to protect his good eye. But the two soon discovered that standard protective visors scratch easily, fog up, and cause visual distortions. Set on helping his son continue playing, the older Jarvis, then chief executive of food distributor Demakes Enterprises Inc. in Lynn, Mass., set out to design a better face guard.

He appears to have succeeded beyond his wildest hopes. Months before they were due to hit stores in early July, Jarvis' One Xcel visors for football and hockey helmets had already racked up strong endorsements from ophthalmologists and sports associations across America. Jarvis also snared plum distribution agreements with sporting goods makers. And he hopes to have a special protective goggle for basketball players ready by next February.

"A SENSE OF PURPOSE." If athletes like what they see, Jarvis' personal mission could have a profound impact on safety in contact sports. It may also pull in millions of dollars for One Xcel Inc., the company that Jarvis started in Danvers, Mass., to develop and market the product. "It wasn't my intention to enter the optical or sporting goods business," says Jarvis, age 45. "I just wanted to provide my son with the right equipment. But I've learned that to have a product, you need a sense of purpose."

It helps, of course, to stumble on a



A NEW EDGE

After his son was blinded in one eye playing basketball, Ed Jarvis quit as CEO of a food distributor to develop and sell nondistorting eye gear

genuine social need. Prevent Blindness America, a nonprofit organization headquartered in Schaumburg, Ill., estimates that nearly 44,000 Americans suffered sports-related eye injuries in 1994. And face guards are potentially the best protection against such injuries.

Unfortunately, even in sports that require helmets, eye protection is inadequate. Jarvis collected plastic visors from different manufacturers and sent them to a private optical laboratory. "They called me back and said that there was no optical design in any of the polycarbonate products," he recalls. The visors were simply pieces of plastic that

were shaped to accommodate helmet

Recognizing the challenge—and the business opportunity—ahead, Jarvis leapt. He sought out experts in optics, ophthalmology, and new materials as consultants, and in January, 1996, launched One Xcel. When he needed cash, venture capitalists at BancBoston Capital Inc. invested more than \$1 million in return for a 50% stake.

With a staff of five and a team of outside experts, Jarvis reinvented sports visors. He varied the outer and inner curvature and thickness of the plastic lenses to reduce distortion and coated them to prevent fogging and scratches. He also expanded the visual area from the customary 180 degree side-to-side to 205 degrees. All that costs money. Prices for football shields could run as high as \$400, about 15% more than other visors. But eye-injury experts say it will be worth the premium. "It's a superior product," declares Dr. Jack Jeffers, team ophthalmologist for the Philadelphia Eagles, who has examined the One Xcel shield.

In fact, One Xcel visors are the only shield used by the National Football League players next fall. Jarvis also has firm endorsements from the American Hockey Coaches Assn. and the National Hockey League. To sell the shields, Jarvis signed exclusive marketing agreements with Karhu U.S.A. Inc., a maker of hockey sticks and other gear, and Riddell Inc., the football helmet supplier.

Will the players go for it? Former New York Ranger Dave Maloney, who coaches youth hockey in Greenwich, Conn., thinks professionals will welcome a shield that doesn't distort vision because "the slightest edge can make a great difference." If it also saves the eyesight of the thousands of sports enthusiasts, Jarvis will consider his success complete.

By Neil Gross
and Greg Greenberg in New York

Risky Business

ACTIVITY	ESTIMATED U.S. SPORTS EYE INJURIES IN 1994
BASKETBALL	9,117
BASEBALL	6,907
POOL ACTIVITIES	4,039
RACQUET SPORTS	2,829
FOOTBALL	2,318
SOCCER	1,330
HOCKEY	922
OTHER ACTIVITIES	16,197
TOTAL	43,659

tual fice
eedPaq 288 ephony Modem
ll Duplex eakerphone*
swering chine*
x chine*
ernet Ready



Speakerphone
operates via phone line
or cellular phone

Just Connect
Communication
Software, create
a point-and-click
virtual office.

The Compaq
PremierSound audio
system. 16-bit
stereo sound in
any configuration.

I want sound. Big, big sound. I want a full duplex speakerphone so they can hear me in Texas.



COMPAQ

EDITED BY KELLEY HOLLAND

AOL'S PRESIDENT LOGS OFF

IT WAS A SHORT-LIVED romance. On June 24, after four months on the job, William Razzouk resigned as president and COO of America Online. The 48-year-old Federal Express veteran was hired early this year to impose some order at the fast-growing online service provider, which is suffering from intensified competition and controversy over its billing practices. AOL's explanation for the abrupt departure: Razzouk's family had second thoughts about leaving Memphis, and CEO Stephen Case wanted a more hands-on role ahead of a planned marketing blitz this fall. But sources close to AOL

said clashes of management styles played a role, as did Razzouk's failure to develop rapport with many on the AOL team. Razzouk couldn't be reached for comment.

CHARITY TELLS PRU: NOT SO FAST

PRUDENTIAL SECURITIES looked smart in the spring of 1995 when it pulled some \$39 million it was owed by the Foundation for New Era Philanthropy out of a margin account New Era had there. But now, the foundation's trustee, Arlin Adams, is suing Pru to force it to give up that money—and more—to help repay charities and creditors stiffed when New Era collapsed. Prudential calls the suit "groundless" and pledges to fight vigorously. Adams sued a day after filing a proposed settlement that would help give charities that lost money with New Era about 65¢ on the dollar.

CLOSING BELL

POWER STRUGGLE

In April, Kansas City Power & Light's courtship with Utilicorp United was abruptly interrupted by a bid from Western Resources. KCP&L declined Western's overtures and Utilicorp upped its bid. Western also increased its offer. On June 25, KCP&L rejected Western's second bid in favor of Utilicorp's lower, friendlier one. Western now vows to tender an offer directly to shareholders. The market is excited—KCP&L has traded above 27, from 23½ in April—but skeptical: at 26½, KCP&L is still trading far below the 31 Western is bidding.



WE'RE EQUALS—REALLY

WHEN IS A MERGER REALLY an acquisition? Bell Atlantic has long insisted that its \$20.5 billion deal for Nynex is a joining of equals, even though it will keep the name Bell Atlantic and make BA Chairman Ray Smith, 58, CEO of the combined company for several years. But under a 1913 antimerger law, making the deal a merger means Congress must approve it. So on June 26, BA announced that it will simply acquire Nynex—sort of. The companies insist that in practice, theirs is still a "merger of equals."

ANOTHER BLOW TO BURMA

MASSACHUSETTS IS TAKING on the repressive regime in Myanmar (formerly known

HEADLINER: THOMAS ENGIBOUS

A 20-YEAR MAN FOR TEXAS INSTRUMENTS

As a Chicago-area high school student in the early 1970s, Thomas Engibous built a digital computer that added numbers by flashing neon bulbs. The project led him into chip engineering and, in 1976, to Texas Instruments. On June 20, the 43-year-old was named president and CEO, replacing Jerry Junkins, who died on May 29 during a business trip to Europe. TI Director James Adams says Engibous stands out as a strategic thinker: "He takes his time on the big decisions and doesn't on the smaller ones."

Engibous is taking over

the Dallas chipmaker at critical time. Tumbling prices are hurting TI's profits, and net income fell 34% from 1994's \$1.1 billion. But he promises radical change anytime soon. "I've been a member of the strategy team since 1993," he points out.

Engibous isn't all engineer. For inspiration, he cruises open water in his 1974 Chris-Craft Commander. "Every time he gets promoted, he buys a bigger boat," jokes pal Walden Rhines, CEO of Mentor Graphics. Does that mean a yacht is in view?

By Gary McWilliam



as Burma). On June 25, the state passed the toughest U.S. sanctions law yet against American companies doing business there. That means some major corporations will be barred from Massachusetts state government contracts. More than \$1 million in business is affected. Six municipalities, including San Francisco, have already enacted similar sanctions. Several companies with direct investments—Texaco, Arco, and Unocal—say their ventures in Myanmar help the cause of freedom more than isolation would.

GERBER BOWS TO MOMS' PLEAS

YUM, YUM. GERBER PRODUCTS is taking the sugar and starch out of 42 kinds of baby food. Chief Executive Al Piergallini says the change is in response to consumer demand for healthier fare for babies and

toddlers. Already, consumers have pushed Gerber's share of the baby-food market down two-thirds, from 71% in 1994. Some of the manufacturing changes required to remove the starch and sugar are decidedly low-tech. For example, by hand-peeling bananas, Gerber can remove the bitter string clinging to the fruit, creating a sweeter mix. Gerber says that eventually, 121 of its baby foods will be free of added starch and sugar.

ET CETERA...

- Saab story: GM has retained an option to buy 50% of Saab it doesn't want.
- The EPA may force additional businesses to report chemical emissions.
- Craig Livingstone, head of the White House secret office, resigned.
- Quaker Oats announced its Snapple business will suffer a loss for the year.

friday
configure 5

Rest

Relaxation

Peace of Mind



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BY OWEN ULLMANN

WILL DICK LAMM BE THE ROSS PEROT OF '96?

The '96 Presidential race may soon have a new entrant who eschews the politics of joy. His bitter message: America is headed for fiscal Armageddon, and neither Bill Clinton nor Bob Dole will sound the alarm.

Meet ex-Colorado Governor Richard D. Lamm—"Governor Gloom," as he was known back home. The registered Democrat hopes to be the nominee of Ross Perot's Reform Party, which will announce its Presidential candidate at an Aug. 18 convention in Valley Forge, Pa. Convinced that the nation is headed for bankruptcy when baby boomers begin to retire, Lamm wants to overhaul Social Security, Medicare, military pensions, veterans programs, and nearly every other budgetary sacred cow Clinton and Dole are afraid to touch. "I'm coming from the most fiscally irresponsible generation in American history," Lamm says. Fixing the budget, he adds, will take an effort "equal to the magnitude of the civil rights movement."

Bold talk, for sure. But while the little-known Lamm has faint chance of taking the White House, his message could dog the two parties in '96. After all, Perot's crusade for a balanced budget in the 1992 campaign pressured Clinton and congressional Republicans to make deficit reduction a top priority. "We need more kamikaze candidates willing to fall on their swords to get the message out," says Steven E. Schier, a political scientist at Minnesota's Carleton College.

SHALLOW POCKETS. Lamm's pain-and-sacrifice agenda sure isn't hurting him with the Perot crowd. His June 1 speech to California's Reform Party set off a groundswell to make him this year's standard-bearer. His ideas include partially privatizing Social Security and raising the retirement age, rationing health care, tightening curbs on immigration, phasing out affirmative action over 10 years, shuttering veterans hospitals, and enacting campaign finance reform.



LAMM: No nod yet from Boss Ross

But will the Texas billionaire let someone else lead a movement he founded and bankrolled? Perot isn't saying. Lamm thinks he would win in a fair fight. Perot "ran a wonderful teach-in in '92 to wake up the country," Lamm says. **BUSINESS WEEK.** Now, he says, most Perotistas "don't think he's the best to take this party to the next stage."

The next stage is to build on Perot's impressive 19% showing in 1992. Polls show Perot below that now because, politicians say, voters believe he's too eccentric. Lamm is more credible. "He's not paranoid like Perot," says Democratic strategist Ted Van Dyk. But then, neither is Lamm a tycoon who can finance his candidacy himself. Raising the \$20 million Lamm estimates he'll need to register voters' radar screens will be very tough.

DOLE'S LOSS? Lamm has other liabilities. In 1984, he provoked a storm by suggesting the terminally ill shouldn't protect their lives and hence their medical costs. And as governor, he was caught in an ethical flap: He parlayed \$5,000 into \$4 million with money that his ex-law partner had vested for him with a Denver stockbroker later convicted of racketeering. Although Lamm was cleared of wrongdoing, he admits the episode is valid to raise "issues saying we have to restore trust in government."

Such candor doesn't win Presidential elections, say those who figure Lamm appeals only to a small group of moderate Republicans and suburban independents. "A vote for Lamm, Ross Perot, or any other third-party candidate is a vote for Bill Clinton," worries one Dole operative. Clinton strategists happily concur. Boldly, Lamm predicts he can win a "principled plurality" of 40%. That's unlikely. But he forces Clinton and Dole to confront critical issues that candidates are trying awfully hard to avoid.

With Douglas Harbrecht and Joseph V...

CAPITAL WRAPUP

CAPITOL CONTACTS

► A few GOP House freshmen hope to bridge the chasm between their rowdy chamber and the more civil Senate. The reason: At least seven of the first-termers were Hill staffers who had worked with Senator Trent Lott, the new Majority Leader. Among the House frosh who've opened back-channel contacts: Roger Wicker of Mississippi, a former Lott aide; Indiana's Mark Souder; New York's Michael Forbes; and George Nethercutt of Washington state.

MAGAZINER'S MISSION

► Presidential adviser Ira Magaziner has a new objective, this one in cyberspace rather than in your doctor's office. Magaziner, who helped shape President Clinton's doomed plan to overhaul the nation's health-care system, is now leading a task force that hopes to establish guidelines for uniform rules around the globe that would keep governments from restricting commerce on the Internet. His aim: Crafting a plan to be implemented in a second Clinton term.

JAPAN LIKES BOB

► Resurgent isolationism in the Republican Party has governments from Bonn to Beijing quietly rooting for President Clinton's reelection. Tokyo is Dole country. Japanese officials say privately that they would prefer to see the White House back the hands of the GOP, which stresses the U.S.-Japan security pact over trade disputes. While Tokyo applauds Treasury Secretary Robert E. Rubin's steady-dollar policy, it resents the Clintonites' stridency in trade talks.



Q. It's midnight on June 1st.
You're in a place where the
temperature chart reads the same,
be it fahrenheit or centigrade.
Where on earth are you?

Can taking a global view help solve your energy problems?

These days, conventional solutions
will not suffice. With energy
markets constantly changing, it's hard
to keep sight of the bigger picture.
Opportunities are immense. But
so are the risks. The question is, which
do you take?
For a clearer view, you could start
talking to us. Enron.

We rate as one of the world's
leading energy companies, involved
in every aspect of the energy business
from exploration through project
development to supply.

But there's something else we
can supply in abundance. Ideas.
The kind of ideas that can redefine
the way you think about energy.

First, we listen. Then we draw
on the spectrum of our experience
to devise a fully integrated solution
specifically tailored to meet your
particular needs.

Supply, finance, risk management
design, construction, operation...
whatever the problem, you can
count on us to offer you a more

creative energy solution

Oh, and about that global question
we posed above. The answer? You'd
be in the Antarctic at a temperature
of minus 40 degrees.

ENRON

CREATING ENERGY
SOLUTIONS WORLDWIDE

THE GLOBETROTTERS TAKE OVER

Worldwide champions outpace domestic competitors



Since BUSINESS WEEK first launched its rankings of the world's most valuable corporations in 1988, the global economy has been transformed. More countries are open to international trade and investment than ever before. For corporate giants, the biggest opportunities are far beyond their home markets.

This year's Global 1000 is a barometer of such change. The rankings show investors are clearly valuing global champions while shunning domestic also-rans. From the U.S. to Europe to Japan, the companies moving up the rankings are those that have become worldwide names in technology, manufacturing, and consumer goods. **"FLUID GAME."** As in recent years, the U.S. is at the center of the action. Corporate America increased its lead in the standings over Japanese and European rivals. The list contains a record 422 U.S. companies, up from 396 last year. Much of this of course is thanks to an American bull market, which sent their combined value up 32%, to \$5.1 trillion. The U.S. now accounts for 46% of the \$11.2 trillion value of the entire Global 1000, compared with just 30% in 1988. And for the first time in the nine-year history of the Global 1000, a

U.S. company—General Electric Co.—ranks No. 1, with a value of \$137.3 billion. Since 1988, GE Chairman John F. Welch has added \$99 billion to the market value of the world's premier blue-chip company (page 48). "This is a very fluid, dynamic game," says Welch.

It's also a very different game from the late '80s, when mighty Japan was rapidly extending its reach. On our first Global 1000, the Japanese companies accounted for 48% of the list's then-\$5.7 trillion value. Together, they were worth

about 60% more than all the U.S. companies on the list. Now, the U.S. giants are worth 95% more than the Japanese counterparts. Japan accounts for just 23% of the Global 1000's value.

In Europe, blue chips such as Siemens, Heineken, and L. M. Ericsson have soared. But because of European anemic recovery, its companies have slipped further behind their U.S. rivals.

Of course, because all companies are ranked in U.S. dollars, some of the shifts reflect currency swings. The Global

1000, compiled by Geneva-based Morgan Stanley Capital International, tracks some 2,000 companies in 21 countries. The publicly traded companies are ranked on a worldwide basis, using market value and other data measured at the end of May each year. This year, the dollar gained ground against the yen, wiping out most of the 30% rise in yen market value posted by Japanese companies.

Still, with the yen worth only about 100 yen to the dollar, more than in 1988, the prominence of U.S. companies in the rankings isn't just a byproduct of currency fluctuations. U.S. officials have been quick to notice this comeback. Says Treasury Secretary Robert E. Rubin, "We're all looking at our companies—in a lot of industries—and saying, 'They have the most competitive economy.'"

The U.S. has done well in information technology

How the Giants Stack Up

SALES

(BILLIONS OF U.S. DOLLARS)

1	GENERAL MOTORS	\$168.8
2	MITSUBISHI CORP.	164.6
3	mitsui & co.	162.1
4	ITOCHU	151.1
5	SUMITOMO CORP.	149.6
6	MARUBENI	143.8
7	FORD MOTOR	137.1
8	EXXON	107.9
9	ROYAL DUTCH/SHELL GROUP	107.8
10	TOYOTA MOTOR	99.2

SHARE-PRICE GAIN

(PERCENTAGE CHANGE FROM 1985 TO U.S. DOLLARS)

1	OMEGA	1,774%
2	ASCEND COMMUNICATIONS	590
3	CASCADE COMMUNICATIONS	431
4	U.S. ROBOTICS	340
5	HFS	314
6	REPUBLIC INDUSTRIES	292
7	TOTAL SYSTEM SERVICES	254
8	AMERICA ONLINE	217
9	FORE SYSTEMS	209
10	CARTNER GROUP	199

PROFITS

(BILLIONS OF U.S. DOLLARS)

1	ROYAL DUTCH/SHELL GROUP	\$6.78
2	GENERAL MOTORS	6.72
3	GENERAL ELECTRIC	6.57
4	EXXON	6.47
5	IBM	6.02
6	AT&T	5.52
7	PHILIP MORRIS	5.48
8	FORD MOTOR	4.14
9	HSBC HOLDINGS	3.82
10	GLAXO WELLCOME	3.79

RETURN ON EQUITY

(PERCENTAGE)

1	GLAXO WELLCOME	1915.0%
2	GENERAL MILLS	302.2
3	INTIMATE BRANDS	184.8
4	AVON PRODUCTS	149.1
5	UST	143.2
6	VASTAR RESOURCES	130.1
7	INVESTOR	104.7
8	SMITHKLINE BEECHAM	78.7
9	FREEPORT-McMORAN COPPER & GOLD	68.5
10	SCHERING-PLOUGH	66.6

DATA: MORGAN STANLEY CAPITAL INTERNATIONAL BUSINESS WEEK

s value jumped 45%, to \$71 billion, as Microsoft Corp. climbed to 12th on the list in 1988, it wasn't even on the Global 1000, which then had a cutoff of \$1.27 billion. Neither was Sun Microsystems, which vaulted to 261 on this year's list up from 644 last year. Netscape Communications Corp., the stock market darling, didn't even go public until last year. Worth \$5.6 billion, it debuted on the Global 1000 at No. 570.

PEAN AGGRESSIVENESS. The computer industry remains brutally competitive. Apple Computer Inc., with the steepest drop of any company, fell from 11th on the list last year to 978, and remains vulnerable to Japanese rivals such as Sony. Still, the Japanese concede the U.S. retains the global lead. "When it comes to software operating systems and microprocessors," says Toshiba President Fumio Sato, "we envy the Americans."

In the U.S. consumer-products companies continue to lead in global markets. Take McDonald's Corp. It's now serving burgers in 115 countries, up from 53 in 1990. McDonald's is worth \$33.7 billion—four times as much as in 1988. Coca-Cola now gets 70% of its sales from overseas. No surprise that it rose to No. 4, with a value of \$115 billion.

Europe, despite the Continent's economic problems, the best companies are displaying a new aggressiveness. In France, Carrefour, the retailer that invented the hypermarket in the '60s, is taking the market globally. With over half its sales abroad, Carrefour rose 66% last year and now ranks 114 on the list, up from 188. "Germany has [also] become a truly two-tier equity market," argues Thomas R. Holmes of Shröder Hengst Research in Frankfurt. Rising export profits made drug companies the big winners this year. Hoechst, up 55%, had the biggest gain, thanks in part to its \$7.1 billion takeover of U.S. drug maker Marion Merrell Dow. Royal Dutch/Shell Group ranks in the world's most valuable oil companies. Following a 19% gain, it ranks 2nd on the Global 1000.

Even in Japan, where the Nikkei is trading 43% below its peak, incentives are rewarding globalization. Despite the problems of the Japanese economy, "they have not been standing still in their targeted industries," says TRW Chairman Joseph T. Gorman. Toyota Motor Corp., which remains the world's most valuable auto company, has nearly doubled its market value since 1988. The Japanese electronics giants remain equal in some. Sony Corp., now preparing a financial assault, rose 32%, to \$23.8 billion last year, up from \$9.7 billion in 1988. It largely because of the rout of

The Top 100 Companies

A number of American companies made strong moves up the list, including General Electric, Coca-Cola, and Microsoft

RANK 1996 1995		MARKET VALUE Billions of U.S. dollars		RANK 1996 1995		MARKET VALUE Billions of U.S. dollars	
1	3	GENERAL ELECTRIC	U.S. 137.34	51	40	AMOCO	U.S. 36.00
2	2	ROYAL DUTCH/SHELL	Neth./Britain 128.29	52	78	ELI LILLY	U.S. 35.50
3	1	NTT	Japan 115.70	53	28	BRITISH TELECOMMS.	Britain 34.34
4	6	COCA-COLA	U.S. 115.07	54	46	ABBOTT LABORATORIES	U.S. 33.90
5	8	BANK OF TOKYO-MITSUBISHI	Japan 110.29	55	23	TOKYO ELECTRIC POWER	Japan 33.79
6	4	EXXON	U.S. 105.27	56	74	AMERICAN HOME PRODUCTS	U.S. 33.73
7	5	AT&T	U.S. 99.72	57	63	FANNIE MAE	U.S. 33.72
8	7	TOYOTA MOTOR	Japan 85.78	58	58	McDONALD'S	U.S. 33.65
9	13	PHILIP MORRIS	U.S. 82.09	59	92	CIBA-GEIGY	Switzerland 31.86
10	16	MERCK	U.S. 78.62	60	57	SIEMENS	Germany 31.37
11	14	ROCHE HOLDING	Switzerland 73.31	61	67	AMERITECH	U.S. 31.36
12	20	MICROSOFT	U.S. 71.04	62	45	HITACHI LTD.	Japan 30.82
13	22	JOHNSON & JOHNSON	U.S. 64.88	63	214	CISCO SYSTEMS	U.S. 30.49
14	10	FUJI BANK	Japan 62.99	64	226	CHASE MANHATTAN	U.S. 30.47
15	21	INTEL	U.S. 62.09	65	55	SBC COMMUNICATIONS	U.S. 30.08
16	11	SUMITOMO BANK	Japan 61.89	66	68	BROKEN HILL PROPRIETARY	Australia 29.42
17	9	INDUSTRIAL BANK OF JAPAN	Japan 60.47	67	91	BOEING	U.S. 29.37
18	19	PROCTER & GAMBLE	U.S. 60.28	68	73	MITSUBISHI HEAVY INDUSTRIES	Japan 28.98
19	17	WAL-MART STORES	U.S. 59.35	69	64	MINNESOTA MINING & MFG.	U.S. 28.57
20	18	IBM	U.S. 57.61	70	107	ASTRA	Sweden 28.09
21	15	DAI-ICHI KANGYO BANK	Japan 56.29	71	65	DAIMLER-BENZ	Germany 28.05
22	12	SANWA BANK	Japan 55.83	72	80	SMITHKLINE BEECHAM	Britain 28.04
23	42	HEWLETT-PACKARD	U.S. 54.30	73	52	ASAHI BANK	Japan 27.93
24	30	PEPSICO	U.S. 52.43	74	95	BANKAMERICA	U.S. 27.54
25	29	BRITISH PETROLEUM	Britain 48.21	75	69	BELL ATLANTIC	U.S. 27.31
26	27	GLAXO WELLCOME	Britain 45.68	76	86	ELECTRONIC DATA SYSTEMS	U.S. 27.27
27	54	PFIZER	U.S. 45.28	77	101	GILLETTE	U.S. 26.31
28	36	DUPONT	U.S. 44.70	78	61	TOKAI BANK	Japan 25.96
29	34	AIG	U.S. 44.69	79	102	VEBA	Germany 25.52
30	26	MOBIL	U.S. 44.51	80	53	SEVEN-ELEVEN JAPAN	Japan 25.39
31	25	NESTLE	Switzerland 44.05	81	87	EASTMAN KODAK	U.S. 25.26
32	41	BRISTOL-MYERS SQUIBB	U.S. 42.99	82	176	LLOYDS TSB GROUP	Britain 25.05
33	50	FORD MOTOR	U.S. 42.87	83	131	CHRYSLER	U.S. 24.92
34	48	SINGAPORE TELECOMMS.	Singapore 42.62	84	70	B.A.T. INDUSTRIES	Britain 24.80
35	51	WALT DISNEY	U.S. 42.18	85	100	HOME DEPOT	U.S. 24.48
36	32	GENERAL MOTORS	U.S. 41.68	86	118	SUN HUNG KAI PROPERTIES	Hong Kong 24.40
37	44	GTE	U.S. 41.63	87	59	UNION BANK OF SWITZ.	Switzerland 24.33
38	49	BELLSOUTH	U.S. 40.38	88	135	NATIONSBANK	U.S. 24.29
39	81	CITICORP	U.S. 40.31	89	126	HUGHES ELECTRONICS	U.S. 24.29
40	39	HSBC HOLDINGS	Britain 40.02	90	NR	LUCENT TECHNOLOGIES	U.S. 24.19
41	38	MOTOROLA	U.S. 39.52	91	141	ING GROEP	Netherlands 24.04
42	62	SANDOZ	Switzerland 39.26	92	105	COLUMBIA/HCA HEALTHCARE	U.S. 23.98
43	47	CHEVRON	U.S. 39.00	93	106	SONY	Japan 23.78
44	NR	ENI	Italy 38.19	94	129	BAYER	Germany 23.55
45	24	SAKURA BANK	Japan 37.91	95	75	ITO-YOKADO	Japan 23.55
46	37	NOMURA SECURITIES	Japan 37.04	96	72	DEUTSCHE BANK	Germany 23.44
47	31	ALLIANZ HOLDING	Germany 36.94	97	160	HONDA MOTOR	Japan 23.43
48	35	UNILEVER	Neth./Britain 36.88	98	66	NIPPON STEEL	Japan 23.39
49	56	BERKSHIRE HATHAWAY	U.S. 36.42	99	104	HUTCHISON WHAMPOA	Hong Kong 23.22
50	43	MATSUSHITA ELECTRIC INDL.	Japan 36.16	100	294	WELLS FARGO	U.S. 23.11

the Nikkei, Japan's less-competitive giants have suffered the biggest losses since 1988. Nippon Telegraph & Telephone Corp. fell to third this year after leading the Global 1000 virtually every year. In 1988, NTT was worth a staggering \$296 billion. But once the stock market bubble burst, investors realized the monopoly was far behind its international rivals. Following a 10% drop this year, NTT is worth \$180 billion less than eight years ago. Most of Japan's

top 20 banks lost ground after posting a record \$14.5 billion cumulative loss.

The losers haven't been confined to Japan. In Europe, Italy's Fiat slid from 117 to 198 on the Global 1000 when it didn't meet profit expectations. British laggard United Biscuit Holdings PLC, which sank to 976 last year from 689 in 1988, finally fell off the list, despite selling troubled cookie unit Keebler Co.

For investors, the question is not rankings themselves but how well a

company competes in its business. Some Japanese exporters are gaining new strength from the weakening yen and will be strong rivals next year. But the highly valued U.S. multinationals are now globally entrenched. Stock market corrections won't affect their course.

By William C. Symonds in Toronto with Brian Bremner in Tokyo, Steven Toy in Paris, Karen Lowry Miller in Bonn, and bureau reports

GE'S WELCH: 'FIGHTING LIKE HELL TO BE NO. 1'

Soon after he won the top spot at General Electric Co. in 1981, Chairman and CEO John F. Welch began talking of turning the American industrial giant into the "most globally competitive" company in the world.

Now, on the basis of how investors value companies, GE has jumped to No. 1 in the world with a market capitalization of \$137.3 billion. Under Welch, the corporate giant has put together a portfolio of products ranging from power-generating equipment and jet engines to financial services that seem to fit the needs of emerging-market nations investing heavily in infrastructure.

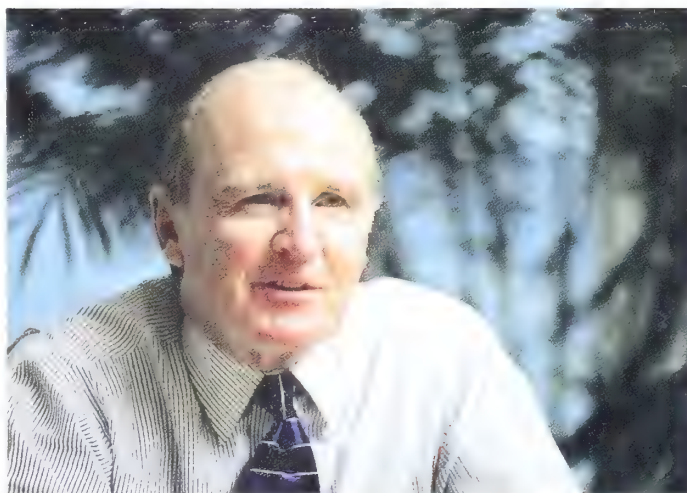
"RAZOR'S EDGE." But any gain like this is fragile. It depends on investors and unpredictable markets. So despite undergoing open-heart surgery last summer, the 60-year-old Welch remains intensely competitive. While pleased with GE's record profits of \$6.6 billion last year, Welch regularly warns his workers against complacency. "Our output per worker is growing, American business across the board is doing a good job," Welch told *BUSINESS WEEK* in an interview on returning from a trip to Europe. But he believes things could easily reverse. "Don't make too much of the moment is all I am saying," Welch says.

Welch closely watches such multinational competitors as Siemens, ABB, Toshiba, and Mitsubishi. He

sees these rivals as viable long-term foes, even though they may suffer from temporary inequalities in their currencies or political and social upheavals at home. "We've just got to be faster," says Welch. "We come to work every day on the razor's edge of a competitive battle."

Indeed, in many of GE's key businesses overseas, deals are won with

cy separated managers from their businesses, so Welch moved to simplify management. He bought RCA and its National Broadcasting Co. unit, sold off the consumer electronics operations, and dramatically expanded into financial services. And he directed a serious push into overseas markets. The company's international sales now equal 40% of GE's



thin bids and political favoritism. Siemens and ABB have aggressively chased power-generation projects in China, while Rolls-Royce has undercut GE for jet-engine orders in Singapore. Still, many foreign chief executives look to GE as a market weather vane. Says Siemens CEO Heinrich von Pierer: "Jack Welch is our benchmark."

It's easy to see why. The GE Welch took over in 1981 was a lumbering giant heavily dependent on industrial businesses, tied to unionized manufacturing and big-ticket orders that rode the waves of the U.S. economy. Layers of bureaucra-

cy separated managers from their businesses, so Welch moved to simplify management. He bought RCA and its National Broadcasting Co. unit, sold off the consumer electronics operations, and dramatically expanded into financial services. And he directed a serious push into overseas markets. The company's international sales now equal 40% of GE's

"We're sitting here fighting like hell to be No. 1 next year," says Welch. Proof, after all, that he didn't get there by coasting.

By Tim Smart in Fairfield, Conn.

BENCHMARK

Foreign CEOs look to emulate General Electric as it slashes debt, boosts productivity, and pushes overseas

total revenues of \$70 billion—up from less than 30% eight years ago—and will probably reach parity with its U.S. sales soon.

Today, Welch is less acquisitive but no less performance-driven. A

THE BUSINESS WEEK GLOBAL 1000

Summary

MARKET VALUE: Share price on May 31, 1996, multiplied by available number of shares outstanding, translated into U.S. dollars at May month-end exchange rates. Market value includes several classes of stock; price and yield data based on the company's widely held issue.

PRICE AND ANNUAL YIELD: Closing per-share price

on May 31, 1996, in U.S. dollars. Annual percent change from May 31, 1995, to May 31, 1996, both in U.S. dollars and in each company's local currency.

PRICE/BOOK VALUE RATIO: The ratio of May closing price to latest available net worth per share or common shareholders' equity investment.

PRICE/EARNINGS RATIO: The ratio of May closing price to latest 12 months' earnings per share.

YIELD: Latest 12 months' dividends per share as a percent of May closing price.

SALES: Net sales reported by company, translated at May 31 exchange rates; revenues for banks and other financial institutions are not included because they are not comparable to those of industrial companies.

PROFITS: Latest aftertax earnings available to common share-

holders, translated at May 31 currency exchange rates; profits are from companies' continuing operations before extraordinary items. Sales, profits, and assets are for 1995 fiscal year unless noted.

RETURN ON EQUITY: Latest 12-months' earnings per share as percent of most recent book value per share.

INDUSTRY CODE: For key to the two-digit code, see page 80.

For individual companies: Morgan Stanley Capital International, unless otherwise indicated. For further information on MSCI data, contact Morgan Stanley & Co. at 212 761-8141 (New York) or 171 425-6660 (London). Country composites and rankings calculated by BUSINESS WEEK. Additional data by Standard & Poor's Compustat, a division of the McGraw-Hill Companies, if footnoted.

RY	GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL	PRICE PER SHARE U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL	PROFITS U.S. \$ MIL	ASSETS U.S. \$ MIL	RETURN ON EQUITY %	INDUSTRY CODE												
BAL COMPOSITE													11202429	150	17	21	3.2	24	2.7	9492812	504300	31580349	17.2	
STRALIA																								
NTRY COMPOSITE													128009	8	27	15	2.2	18	4.2	67689	9805	473183	13.4	
BROKEN HILL PROPRIETARY	66	29421	15	19	7	3.1	24	2.7	14164	1291	24183	13.0	11											
NEWS CORP.	181	15958	6	6	-5	1.3	16	0.4	9721	1072	24105	8.2	51											
NATIONAL AUSTRALIA BANK	215	13655	9	10	-1	1.5	9	7.3	NA	1546	117434	17.2	61											
WESTPAC BANKING	350	8875	5	27	14	1.4	10	5.3	NA	778	84504	13.6	61											
WMC	365	8430	8	42	28	2.6	27	2.4	1639	281	4883	9.8	24											
COMMONWEALTH BANK OF AUSTRALIA	385	8066	8	23	11	1.5	9	8.2	NA	807	79522	16.3	61											
AUSTRALIA & NEW ZEALAND BANKING GROUP	462	6741	5	28	15	1.5	8	6.3	NA	761	89895	18.0	61											
COCA-COLA AMATIL	607	5405	11	88	70	3.4	49	1.4	2370	109	3714	6.9	43											
CRA (3)	NR	5321	16	30	18	3.0	15	3.2	9334	1441	15779	20.7	24											
AMCOR	765	4241	7	-8	-17	1.7	13	4.4	5266	321	5641	13.6	23											
COLES MYER	810	3945	4	19	7	2.0	15	4.8	13415	331	5245	13.8	54											
WOODSIDE PETROLEUM	839	3817	6	38	24	4.1	34	1.7	486	112	2520	12.1	11											
LEND LEASE	853	3708	16	19	8	1.8	17	4.4	1165	208	2779	10.7	64											
FOSTERS BREWING GROUP	886	3571	2	23	11	1.9	15	4.8	3491	275	4906	12.7	43											
CSR	887	3565	4	15	4	1.4	14	6.3	4902e	256e	5728	10.0c	71											
COMALCO	950	3290	6	58	42	2.7	15	3.4	1736	216	2345	17.9	24											
STRIA																								
NTRY COMPOSITE													5784	93	14	24	2.1	46	1.0	NA	131	60635	4.6	
BANK AUSTRIA	556	5784	93	14	24	2.1	46	1.0	NA	131d	60635d	4.6	61											
LGUIM																								
NTRY COMPOSITE													59500	266	13	22	1.7	15	4.1	46149	4611	599618	11.7	
ELECTRABEL	253	11657	215	2	11	1.7	13	6.7	6867	914	14772d	13.7c	12											
PETROFINA	452	6898	297	-1	7	1.8	19	3.8	17908	362	10740	9.5	11											
TRACTEBEL	521	6099	443	22	33	2.0	18	3.5	10238	342	20203d	11.3c	71											
GENERALE DE BANQUE	633	5194	347	10	20	1.5	12	4.7	NA	435	150689	12.8	61											
SOCIETE GENERALE DE BELGIQUE	635	5186	73	2	10	1.0	18	5.0	NA	291	8910	5.5	71											
FORTIS AG (6)	NR	5052	134	25	36	1.9	14	2.6	NA	808	160623	13.9	63											
SOLVAY	656	4986	598	8	17	1.7	13	3.9	8692	392	8402d	13.0c	22											
KREDIETBANK	753	4280	291	21	32	1.5	12	3.4	NA	365	97809	13.1	61											
BANQUE BRUXELLES LAMBERT	880	3595	184	16	25	1.4	13	4.0	NA	284	102544	11.2	61											
POWERFIN	938	3331	139	26	36	1.7	14	3.5	NA	245	2245d	12.4c	12											
GROUPE ROYALE BELGE	984	3220	201	8	17	2.0	17	4.1	2444d	173d	22681d	11.8c	63											

Non-consolidated results. a) Results are for 18 months. b) Results are for 14 months. c) Difference between earnings and book value between 12 and 18 months. d) Based on 1994 data. e) Based on 1995 data. f) Results are for 12 months. g) Results are for 4 months. h) Results are for 10 months. i) Individual ranking calculated for Royal Dutch/Shell group by combining market value of the Netherlands' Unilever NV and Britain's Unilever PLC. j) Global ranking calculated for RTZ-CRA by combining market value of Britain's RTZ and Australia's CRA. k) Global ranking calculated for ABB Asea Brown Boveri by combining market value of Sweden's ABB AB and Switzerland's ABB AG. l) Global ranking calculated for Reed Elsevier by combining market value of Britain's Reed International and the Netherlands' Elsevier. m) Global ranking calculated for Fortis by combining market value of Belgium's Fortis AG Group and the Netherlands' Fortis AMEV. n) Data for this company provided by Standard & Poor's Compustat. Unless otherwise noted, all other data provided by Morgan Stanley Capital International. LOSS = Negative ratio. NA = Not available. NEG = Negative return. NM = Not meaningful.

COUNTRY RANK	GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %		
BRITAIN													
COUNTRY COMPOSITE		983815	9	18	21	6.9	15	3.9	783842	74279	2641516	42.1	
1	BRITISH PETROLEUM	25	48,100	9	22	25	2.6	14	3.7	55943	3120	50126	18.9
2	SHELL TRANSPORT & TRADING (1)	NR	47,400	14	16	19	2.0	17	4.5	107830	6779	117700	11.6
3	GLAXO WELLCOME	36	45,600	13	13	16	323.8	17	4.5	16253a	3785a	13233	1915.0
4	HSBC HOLDINGS	46	40,200	15	16	19	1.9	10	4.1	NA	3815	351432	18.5
5	BRITISH TELECOMMUNICATIONS	53	34343	6	-12	-10	1.8	11	6.4	21521	2682	33249	16.2
6	SMITHKLINE BEECHAM	7	28041	10	28	42	15.1	19	2.8	10863	1433	12632	78.7
7	LLOYDS TSB GROUP	NR	25053	5	26	29	3.8	12	4.4	NA	2006	204133	31.6
8	B.A.T. INDUSTRIES	84	24796	8	3	5	3.5	11	5.8	23085	2209	61953d	32.2c
9	ZENECA GROUP	115	21109	11	43	47	7.0	22	2.8	7589	908	7891	31.5
10	MARKS & SPENCER	116	20074	7	9	12	3.5	20	3.1	11205e	1011e	8841	17.5c
11	REUTERS HOLDINGS	133	19502	12	56	60	12.8	29	1.6	4188	641	3261	44.1
12	BARCLAYS BANK	144	18437	12	9	11	1.7	10	4.3	NA	1917	261579	17.5
13	BTR	156	17582	4	-20	-18	4.9	11	6.5	15150	1487	15316	45.3
14	NATIONAL WESTMINSTER BANK	177	17167	10	13	16	1.6	9	5.1	NA	1824	257738	17.7
15	RTZ (3)	NR	16558	16	22	25	3.1	15	3.3	9334	1441	15779	20.3
16	GENERAL ELECTRIC CO.	183	15875	6	14	17	3.1	18	3.9	16005	874	9781	17.1
17	UNILEVER PLC (2)	NR	15164	19	-4	-2	4.2	15	3.1	49814	2328	30118	27.8c
18	CABLE & WIRELESS	197	15141	7	3	5	2.9	17	2.8	8548e	903e	12202	17.4c
19	HANSON	194	14487	3	-21	-19	2.7	9	8.0	17328	1413	36617	29.9
20	GRAND METROPOLITAN	206	14213	7	7	10	2.6	15	4.3	12434	1012	15152d	17.5c
21	GUINNESS	211	13884	7	-5	3	2.2	14	4.0	7253	1037	12772	15.6
22	BRITISH GAS	217	13448	7	-39	-37	1.1	10	9.5	13326	1399	26970	11.7
23	PRUDENTIAL	226	13158	7	23	26	11.1	11	4.6	13199	1174	97089d	42.3
24	VODAFONE GROUP	243	12073	4	21	24	9.5	31	1.8	1786	368	2184	30.8
25	THORN EMI	247	11941	28	41	45	13.1	24	2.6	6984	413	5035	54.8
26	BRITISH SKY BROADCASTING GROUP	248	11931	7	64	68	-10.0	37	1.4	1205	212	606	NA
27	ABBAY NATIONAL	267	11304	9	14	16	1.9	11	4.9	NA	1058	159793	17.3
28	J. SAINSBURY	270	11104	6	-14	-12	2.2	14	3.8	20915e	797e	9036	15.6c
29	BASS	272	11129	18	36	40	1.9	18	3.6	7036	589	10184	10.9
30	GRANADA GROUP	282	10801	13	36	40	8.5	20	1.8	3689	373	3041	42.6
31	GREAT UNIVERSAL STORES	290	10589	11	8	11	1.9	19	2.9	5213	575	7094	10.0
32	TESCO	309	10048	5	0	2	1.8	13	4.0	20186e	722e	9631e	13.5
33	REED INTERNATIONAL (5)	NR	9769	17	24	28	6.1	22	2.7	5654	855	8520	28.2
34	STANDARD CHARTERED	323	9676	10	78	82	3.5	14	2.1	NA	676	60324	24.8
35	IMPERIAL CHEMICAL INDUSTRIES	326	9576	13	5	7	1.6	11	4.4	15911	860	14676	14.1
36	NATIONAL POWER	342	9115	8	9	12	2.4	10	5.5	6117e	942e	7197	24.2c
37	BOOTS	344	8773	9	15	18	2.9	17	3.6	6675	559	5270	16.9
38	BRITISH AIRWAYS	369	8335	9	15	16	2.2	11	3.0	12023e	733e	15558e	19.0
39	RENTOKIL GROUP	374	7919	6	52	56	17.6	29	1.3	1305	116	871	61.1
40	BAA	398	7831	8	1	1	1.8	16	2.7	1796	432	6616	11.1
41	ALLIED DOMECO	407	7758	7	10	-7	2.2	15	6.4	13828a	874a	9929	14.2
42	CADBURY SCHWEPES	424	7429	7	-1	2	3.9	15	4.1	7400	465	7119	25.3
43	BOC GROUP	450	6937	14	14	17	2.7	17	3.6	5491	386	6759	15.9
44	VENDOME LUXURY GROUP	455	6848	10	22	25	4.0	22	2.0	2015	299	2597	17.7
45	RANK ORGANISATION	473	6599	5	14	17	2.4	19	4.3	4050b	403b	5163	12.5
46	ROYAL BANK OF SCOTLAND GROUP	480	6410	8	26	29	2.7	11	4.1	NA	545	79088	23.6
47	SCOTTISH & NEWCASTLE BREWERIES	494	6288	10	18	19	2.1	18	3.4	5132	408	5024	11.5
48	KINGFISHER	500	6319	9	30	33	3.2	19	3.3	5182e	326e	5087e	16.4
49	COMMERCIAL UNION ASSURANCE	501	6211	9	4	2	1.0	12	5.8	13398	536	87239	8.0
50	ARGYLL GROUP	507	6232	5	4	6	2.5	15	4.3	9009	402	5048	15.1
51	SIEBE	512	6190	12	40	44	3.8	21	1.8	3325	248	4034	18.0
52	PEARSON	542	5964	11	11	14	4.6	24	3.0	2836	95	3978	19.2
53	BRITISH AEROSPACE	551	5858	14	11	10	6.2	18	1.8	8895	522	12197d	34.2c
54	LLOYDS ABBEY LIFE	573	5623	8	11	12	2.3	18	5.2	2349	411	20465	16.9
55	POWERGEN	581	5511	8	0	3	2.0	9	5.1	4544e	638e	5503	21.9c
56	UNITED NEWS & MEDIA	602	5411	12	35	39	5.9	20	3.9	1659	143	1133d	30.0c
57	WHITBREAD	604	5411	11	26	22	1.5	17	3.7	4261e	322e	5039	9.2c
58	LEGAL & GENERAL GROUP	609	5399	11	38	41	4.1	18	4.3	4585	302	58959	46.0
59	GKN	612	5306	15	54	58	3.7	17	3.0	5120	309	3797	21.6
60	BRITISH STEEL	625	5332	4	16	2	0.8	5	6.2	7412	725	9659	17.8
61	ASDA GROUP	623	5283	2	37	41	2.3	16	2.5	8189	265	4403	13.0
62	ASSOCIATED BRITISH FOODS	624	5283	6	16	19	1.5	13	2.1	7583	387	5237	11.7
63	ROLLS-ROYCE	645	5084	3	17	20	2.4	22	2.8	5573	220	5663	11.1
64	LAND SECURITIES	647	5075	10	0	3	0.9	18	4.9	NA	278	8493	5.0
65	SUN ALLIANCE & LONDON INSURANCE	652	5015	6	10	13	1.2	8	5.4	7488	609	18575	14.1
66	GENERAL ACCIDENT	662	4947	10	1	8	1.0	12	5.8	6831	592	30587	8.7
67	BANK OF SCOTLAND	677	4922	4	22	25	2.2	10	3.2	NA	484e	68327e	21.0
68	PENINSULAR & ORIENTAL STEAM NAVIGATION	669	4902	8	-17	-15	1.3	14	7.3	10181	354	11244	9.6

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THE BUSINESS WEEK GLOBAL 1000

COUNTRY	1000 RANK	MARKET VALUE \$ MIL	PRICE U.S. \$	CHANGE P.M. (U.S. \$) (LOCAL)	PRICE/BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL	PROFITS U.S. \$ MIL	ASSETS U.S. \$ MIL	RETURN ON EQUITY %	
69 NATIONAL GRID GROUP	704	4769	3	NA	NA	3.0	8	7.0	2213	584	4735	NA
70 UNITED UTILITIES	791	4724	4	1	1	1.0	7	6.2	2849e	348e	5589	13.5e
71 TOMKINS	700	4679	4	2	5	3.1	14	4.4	5772	321	3407	22.0
72 RECKITT & COLMAN	711	4559	11	2	5	3.0	15	3.6	3645	299	4239	21.6
73 ORANGE	715	4548	1	NA	NA	NA	NA	0.0	354	-218	1244	NA
74 CARLTON COMMUNICATIONS	744	4471	7	15	15	5.5	17	2.6	2447	233	2012	32.6
75 ROYAL INSURANCE HOLDINGS	745	4329	7	24	27	1.0	7	4.7	7054	607	35870	14.8
76 3I GROUP	764	4161	7	21	25	1.0	39	2.1	NA	92	5501	3.3
77 SCOTTISH POWER	785	4080	5	-7	-5	2.3	9	6.1	3519e	507e	2858	27.6e
78 SCHROEDERS	788	4075	1	16	16	3.1	19	1.5	NA	215	18107	16.4
79 BLUE CIRCLE INDUSTRIES	799	3997	5	14	16	2.4	16	4.4	2750	242	3949	14.7
80 WOLSELEY	807	3964	1	23	26	4.0	16	2.7	5863	253	2908	25.1
81 RMC GROUP	827	3870	16	8	-6	1.8	13	3.1	6378	256	5544	14.1
82 TI GROUP	831	3853	8	17	4	6.7	21	3.1	2739	188	2014	30.2
83 GUARDIAN ROYAL EXCHANGE	833	3717	4	28	12	1.2	3	4.2	5851	1052	28600	34.4
84 THAMES WATER	834	3711	1	13	16	1.2	5	5.0	1810	417	5285	14.5
85 ENTERPRISE OIL	871	3625	7	12	14	3.0	26	4.2	1182	133	3899	11.6
86 SEVERN TRENT	914	3430	9	3	6	1.0	7	5.4	1668	309	5717	13.3
87 LADBROKE GROUP	916	3410	3	1	3	1.2	25	4.0	5961	135	5368	4.9
88 SMITH & NEPHEW	917	3414	3	16	19	5.4	18	3.5	1590	187	1276	30.1
89 LUCAS INDUSTRIES	941	3323	4	26	29	3.1	88	3.6	4543	-46	3539	NEG
90 SMITHS INDUSTRIES	955	3270	11	32	35	9.0	21	2.7	1193	145	987	44.8
91 NEXT	957	3266	14	63	67	3.0	14	2.6	1199e	138e	903e	24.7
92 BURMAH CASTROL	964	3211	10	10	13	3.1	16	4.0	4713	208	3565	19.6
93 BURTON GROUP	969	3253	2	66	70	2.4	30	1.9	2911	108	2391	8.3
94 DIXONS GROUP	974	3237	8	97	102	6.3	27	1.9	2552	102	1633	23.7
95 REDLAND	979	3230	6	-10	-7	1.6	13	5.2	4255	246	5369	11.9
96 ARGOS	981	3228	11	67	71	9.4	25	2.4	2225	108	1338	37.9
97 COOKSON GROUP	985	3215	5	23	27	2.9	10	3.3	2789	173	2063	17.7

CANADA

COUNTRY COMPOSITE		170065	30	25	25	2.6	26	2.4	104573	8970	750394	12.6	
1	NORTHERN TELECOM	209	10000	54	41	41	3.6	30	1.0	10672	445	9442	12.2
2	SEAGRAM	226	12918	15	15	1.4	75	1.7	8935e	104e	21355e	1.8	
3	BCE (BELL CANADA ENTERPRISES)	237	12540	40	27	27	1.7	24	5.0	17960	530	28224	7.0
4	BARRICK GOLD	266	11318	32	26	26	3.8	38	0.4	1282	292	3556	10.0
5	THOMSON	319	9729	16	17	17	2.5	20	3.4	7225	469	9981	12.6
6	IMPERIAL OIL	382	8111	43	12	12	1.9	21	3.4	6888	375	8790	9.0
7	ROYAL BANK OF CANADA	418	7493	24	8	8	1.5	4.2	NA	920	133950	16.8	
8	ALCAN ALUMINIUM	427	7386	33	10	11	1.6	16	1.8	9287	543	9702	11.0
9	PLACER DOME	445	7045	10	10	17	4.6	164	1.0	1029	74	2574	2.8
10	CANADIAN PACIFIC	446	7017	20	20	1.6	1.7	1.7	706	-453	11696	NEG	
11	CANADIAN IMPERIAL BANK OF COMMERCE	459	6806	36	1.3	1.3	3.5	NA	740	130735	13.8		
12	BANK OF MONTREAL	508	6224	24	14	14	1.4	4.4	NA	719	110743	16.8	
13	NEWBRIDGE NETWORKS	534	6008	72	103	103	12.0	43	0.0	584	137	603	27.7
14	BANK OF NOVA SCOTIA	572	5401	24	14	14	1.3	4.1	NA	639	107355	15.0	
15	NORANDA	593	5473	22	11	11	1.6	15	3.4	6143	380	9401	10.5
16	TORONTO-DOMINION BANK	603	5411	18	20	20	1.3	9	4.0	NA	579	79360	15.5
17	PANCANADIAN PETROLEUM	674	4864	10	9	3.1	1.5	1.5	1350	166	3302	11.1	
18	IMASCO	693	4720	20	11	11	2.0	1.7	6302	398	40920	16.8	
19	BOMBARDIER	698	4693	14	26	26	1.0	1.0	5196e	225e	4694e	18.8	
20	NOVA	706	4615	10	8	1.7	1.7	2.7	3269	512	6765	14.4	
21	FALCONBRIDGE	804	3979	23	20	20	3.1	18	1.3	1695	243	2117d	17.8e
22	INCO	844	3773	33	30	30	2.4	19	1.2	3471	227	4693	12.7
23	SHELL CANADA	854	3704	10	0	0	1.5	13	4.0	3685	381	4486	11.6
24	PETRO-CANADA	903	3487	38	1.4	1.4	1.6	1.1	3516	181	4732	8.8	
25	CAMECO	993	3194	51	66	66	2.8	33	2.8	288	74	1216	8.7

DENMARK

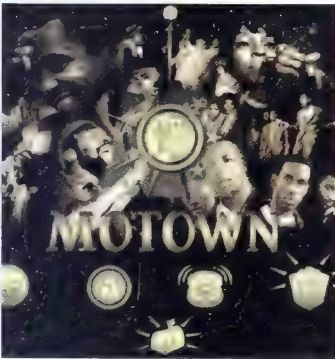
COUNTRY COMPOSITE			31284	7856	14	22	6.9	50	1.8	11088	1874	81464	17.0
1	TELE DANMARK	487	6436	49	-13	-7	1.5	11	5.5	3539	592	6381	13.3
2	NOVO-NORDISK	640	5148	137		38			0.6	2325	265	3538	11.4
3	DAMPSKIBSSKABET SVENBORG	676	4848	32528			14.7	126		NA	38d	446d	11.7
4	DAMPSKIBSSKABET AF 1912	688	4757	22024			18.0	151	0.4	NA	32d	382d	11.9
5	CARLSBERG	879	3603		19	27	2.7	21	1.0	2892	170	3151	12.8
6	DEN DANSKE BANK	945	3309	63	-2		0.8		4.3	NA	615		15.7
7	SOPHUS BERENDSEN	1000	3183	133	46	56	8.2	20	0.6	2332	162	1495	42.1

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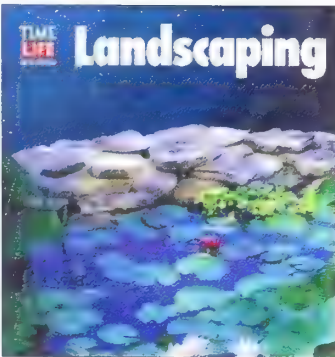
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COUNTRY RANK	GLOBAL RANK	MARKET VALUE U.S. \$ MIL	PRICE PER SHARE \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	P/E RATIO	YIELD %	SALES U.S. \$ MIL	PROFITS U.S. \$ MIL	ASSETS U.S. \$ MIL	RETURN ON EQUITY %			
FINLAND													
COUNTRY COMPOSITE		18154	31	-6	3	2.9	11	3.2	19396	1992	21083	24.3	
1	NOKIA	274	13010	43	-6	2	4.7	18	1.5	7799	861	6971	25.9
2	UPM-KYMMENE	41	5144	19	-5	4	1.0	5	5.0	11597	1131	14112	22.7
FRANCE													
COUNTRY COMPOSITE		342524	126	13	17	2.4	20	3.0	511668	7384	2005481	10.6	
1	LVMH MOET HENNESSY LOUIS VUITTON	113	21149	40	28	3.6	27	2.3	5752	782	12109	13.3	
2	CARREFOUR	114	21027	47	66	7.1	40	1.1	27936	520	12488	17.4	
3	ELF AQUITAINE	141	19578	72	-10	-7	1.4	20	5.2	40238	973	46788	6.7
4	L'OREAL	142	18676	804	16	20	4.3	31	1.3	10310	608	9097	13.8
5	TOTAL	161	17059	72	17	21	1.7	24	3.5	26240	715	26845	7.3
6	ALCATEL ALSTHOM	214	13698	91	0	4	2.1	-3	2.5	30989	-4942	49391	NEG
7	COMPAGNIE GENERALE DES EAUX	232	12693	107	-3	1	2.3	-18	3.1	31481	712	44782	NEG
8	L'AIR LIQUIDE	262	11511	174	11	15	2.8	22	2.3	6218	514	8178	12.5
9	AXA	283	10739	57	10	15	1.5	18	3.3	NA	527	182273	8.2
10	COMPAGNIE DE SAINT-GOBAIN	287	10654	127	2	6	1.3	13	3.8	13583	814	18640	10.3
11	GROUPE DANONE	286	10413	146	11	8	1.5	17	3.2	15348	605	18011	8.9
12	SOCIETE GENERALE	337	9289	16	9	6	0.9	13	4.4	NA	737	308621	7.2
13	RHONE-POULENC	391	8010	25	4	8	1.3	20	3.5	16380	412	26158	6.3
14	SANOFI	395	7905	77	48	54	2.3	26	2.4	4449	304	6549	8.9
15	PARIBAS	434	7291	61	-5	1	0.9	25	5.7	NA	291	257673	3.8
16	BANQUE NATIONALE DE PARIS	438	7222	37	-24	21	0.8	21	2.8	NA	344	280530d	3.6c
17	PEUGEOT	449	6970	139	-8	-4	0.7	21	1.0	31730	329	27991	3.1
18	PINAULT-PRINTEMPS-REDOUTE	461	6920	309	42	48	2.8	24	2.3	15029	293	10473	11.7
19	RENAULT	479	6524	27	16	13	0.8	16	3.7	35558	413	43080	5.0
20	ROUSSEL UCLAF	503	6304	51	62	69	3.7	22	1.9	3181	277	3152	16.7
21	COMPAGNIE DE SUEZ	518	6150	39	-25	-21	0.8	-8	6.2	NA	-765	121781	NEG
22	GROUPE SCHNEIDER	519	6144	46	18	23	2.0	39	2.5	11479	158	11812	5.1
23	UNION DES ASSURANCES DE PARIS	522	6081	20	30	27	0.9	15	4.4	30413	-399	173952	NEG
24	LAFARGE	527	6066	66	-11	-8	1.4	13	4.4	6417	454	9722	10.1
25	CHRISTIAN DIOR	547	5922	141	50	56	1.5	19	2.9	5949	318	18617	8.1
26	MICHELIN	553	5799	50	11	15	2.6	11	1.6	12771	540	13606	24.3
27	LYONNAISE DES EAUX-DUMEZ	574	5601	47	-5	1	1.8	32	3.4	19051	175	30308	5.7
28	HAVAS	585	5411	85	5	9	2.4	32	2.9	8621	171	6591	7.5
29	CANAL PLUS	610	5393	245	84	91	3.9	37	2.4	1962	145	3130	10.4
30	LEGRAND	666	4910	177	17	22	5.0	28	1.3	2130	178	3111	18.1
31	PROMODES GROUP	674	4860	261	13	17	4.0	24	1.3	19429	197	8352	17.1
32	CETELEM	714	4633	218	40	46	2.8	21	1.3	NA	219	15047	13.2
33	ALCATEL CABLE	735	4401	40	23	28	3.7	-9	1.6	7739	-492	7058	NEG
34	SYNTHELABO	772	4179	87	59	66	4.9	27	1.5	1800	153	1563	18.0
35	ACCOR	776	4162	144	12	17	1.7	77	4.0	5991	54	10573	2.2
36	ERIDANIA BEGHIN-SAY	789	4066	156	3	7	1.2	10	6.1	9815	394	8734	12.0
37	USINOR SACLOR	819	3900	16	NA	NA	0.8	5	7.2	15150	856	13951	18.4
38	VALEO	846	3755	54	-2	2	2.0	19	1.4	4874	195	4157	10.3
39	GROUPE PERNOD RICARD	855	3701	66	2	6	2.2	17	3.5	3078	221	3665	13.0
40	AGF	869	3632	27	-26	-23	0.8	17	4.1	14955	209	68871	4.9
41	HERMES INTERNATIONAL	926	3395	78	104	112	5.0	44	0.6	739	78	714	20.7
42	CREDIT COMMERCIAL DE FRANCE	930	3349	48	5	9	1.2	14	3.0	NA	238	66429	8.2
43	PECHINEY	948	3294	47	-27	-24	1.0	9	2.3	14883	283	10908	11.1
GERMANY													
COUNTRY COMPOSITE		406574	346	10	19	3.2	24	2.9	651313	12990	2332403	13.4	
1	ALLIANZ HOLDING	42	36942	1658	4	4	4.0	45	0.9	36617d	629d	167032d	9.0
2	SIEMENS	60	31369	56	18	28	2.4	22	2.2	58112	1214	53669	11.0
3	DAIMLER-BENZ	71	28048	546	13	22	3.3	-7	0.0	67792	-3479	59930	NEG
4	VEBA	79	25520	52	38	49	2.3	18	3.0	43421	1254	44362	12.7
5	BAYER	74	23553	334	46	49	2.1	15	4.2	29186	1567	29000	14.3
6	DEUTSCHE BANK	96	23441	3	4	4	1.7	16	3.6	NA	1391	449862	11.0
7	HOECHST	132	19434	24	56	67	2.6	21	3.7	34160	1119	34493	12.1
8	RWE	134	19495	39	17	26	4.6	22	3.3	41628	711	47956	20.6
9	BASF	165	16926	278	40	40	1.5	11	4.7	30265	1618	27520	13.7
10	MUNCHENER RUCK.	197	14582	1630	1	9	5.1	37	0.8	16892	180	76831	13.7
11	SAP	208	13950	137	9	18	18.4	75	0.9	1199d	183d	1146d	24.5
12	MANNESMANN	241	12719	347	19	28	3.1	25	1.5	21011	349	14861	12.4
13	VOLKSWAGEN	259	12447	352	14	46	1.8	24	1.6	57690	232	55046	7.3
14	DRESDNER BANK	268	1244	1	-10	-3	1.3	17	5.0	NA	652d	257366d	7.5
15	BMW	279	10854	550	3	11	2.1	21	2.3	30210	453	26742	10.2
16	VIAG	302	10230	389	8	14	1.9	16	2.9	27690	757	28217	12.0



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		SALES U.S. \$ M.	PROFITS U.S. \$ M.	1994 U.S. \$ M.	RETURN ON EQUITY								
17	COMMERZBANK	389	208	1.1	NA	6.1	NA	602	264078	NA			
18	BAYERISCHE VEREINSBANK	423	7434	28	-3	1.2	17	5.0	NA	362	232415	7.3	
19	BAYERISCHE HYPOTHEKEN- UND WECHSEL-BANK	4667	6467	1.2	16	5.4	NA	432	192222	7.0			
20	MERCK KGAA	505	6244	38	NA	3.2	3706d	168d	4372d	NA			
21	HENKEL	520	6131	420	2.7	19	2.6	238	7607	14.1			
22	VEW	536	300	-8	0	5.8	28	2.8	118d	8488d	20.9		
23	DEUTSCHE LUFTHANSA	550	5603	15	24	2.6	NA	2.7	12332d	191d	11875d	NA	
24	THYSSEN	5785	185	-2	6	2.0	12	5.1	25613	490	16413	16.7	
25	LINDE	611	5393	642	9	2.3	25	2.3	5423	211	4958	9.2	
26	SCHERING	638	5150	9	18	2.5	27	1.9	3042	163	4691	5.8	
27	BANKGESELLSCHAFT BERLIN	643	15	-8	0.9	10	4.8	NA	269d	19934d	3.8		
28	GEHE	643	56	69	3.9	40	1.5	9952d	90d	3144d	9.7		
29	PREUSSAG	822	3884	255	-15	-8	2.0	14	3.7	17253	243	9857	14.2
30	BEIERSDORF	822	3885	918	22	32	4.2	28	1.7	3499	145	2309	13.1
31	MAN	822	3720	258	-3	1.8	17	3.4	12178	122	8216	10.3	
32	ADIDAS	923	75	NA	9.0	18	0.3	2292	160	1164	50.7		
33	KAUFHOF	956	3362	352	5	14	2.7	31	3.2	13901	90	6026	8.7
34	KARSTADT	956	3305	393	-3	2.1	62	3.1	17747d	26d	7232d	3.3	
35	FRIED. KRUPP AG HOESCH-KRUPP	956	3268	6	14	2.3	14	2.2	13346d	-6d	10929d	15.8	

HONG KONG

COUNTRY COMPOSITE			194733	5	26	26	2.6	17	3.1	29512	11913	186242	16.6
1	SUN HUNG KAI PROPERTIES	86	24397	10	41	41	1.9	18	2.7	2565	1339	16655	10.7
2	HUTCHISON WHAMPOA	86	23219	6	27	27	3.1	19	2.4	4527	1236	15437	16.3
3	HONG KONG TELECOMMUNICATIONS	122	20973	2	-12	NA	16	4.7	3800e	1284e	4724e	44.9	
4	HANG SENG BANK	122	35	35	3.6	20	3.6	NA	1032	4461	18.6		
5	CHEUNG KONG HOLDINGS	163	17000	7	50	50	2.4	11	2.1	1567	1438	9445	21.4
6	SWIRE PACIFIC	207	14086	9	15	15	1.5	17	2.3	6935	834	17883	9.0
7	HENDERSON LAND DEVELOPMENT	238	12431	35	35	2.6	13	3.2	NA	908	8781	19.6	
8	CHINA LIGHT & POWER	329	5	-13	-13	3.9	12	3.6	2206	733	3997	32.1	
9	CITIC PACIFIC	354	8767	4	58	58	2.4	21	1.7	1400	397	5090	11.5
10	WHARF (HOLDINGS)	367	8369	17	18	0.9	18	3.5	875	466	13450	4.9	
11	NEW WORLD DEVELOPMENT	378	8151	5	1.2	1.2	18	2.9	NA	411	10352	6.9	
12	HONGKONG ELECTRIC HOLDINGS	424	6476	3	-10	-10	3.2	12	4.5	897	541	3952	26.9
13	CATHAY PACIFIC AIRWAYS	424	5294	2	27	27	2.4	14	3.4	3936	385	6828	17.3
14	HONG KONG & CHINA GAS	590	4746	2	22	22	3.3	22	2.8	550	211	2024	14.8
15	WHEELOCK & CO.	786	4077	2	14	14	0.7	11	2.4	NA	298	6444	6.5
16	BANK OF EAST ASIA	942	3804	41	41	2.9	18	3.0	NA	212	12025	14.8	
17	HYSAN DEVELOPMENT	942	3316	3	38	38	0.9	21	4.2	254	195	4545	1.4

IRELAND

COUNTRY COMPOSITE		10420	7	30	33	2.4	12	2.9	3033	955	70365	20.9
1 ALLIED IRISH BANKS	867	3640	5	14	17	2.0	10	3.8	NA	363	37897	19.9
2 CRH	922	3403	9	49	3.1	17	1.5	3033	200	2833	18.6	
3 BANK OF IRELAND	928	3377	28	31	2.1	3.4	NA	392e	29635	24.2c		

ITALY

COUNTRY COMPOSITE	168707	10	14	8	2.5	25	2.0	177646	9538	739373	11.3	
1 ENI	44	38189	5	NA	NA	2.8	14	2.9	36177	2795	57335	20.3
2 ASSICURAZIONI GENERALI	138	19078	24	-2	-7	3.2	42	1.0	19897	449	66779d	7.5
3 STET	171	17814	14	17	1.8	20	2.4	14144	943	47340d	9.1c	
4 TELECOM ITALIA MOBILE (TIM)	171	16365	2	NA	NA	NA	36	0.7	1809f	226f	NA	NA
5 TELECOM ITALIA	198	14566	2	36	29	1.3	3.9	19437	1127	40045d	8.7c	
6 FIAT GROUP	198	14566	-11	-16	1.4	12	1.8	48898	1387	61825d	10.9c	
7 ISTITUTO NAZIONALE DELLE ASSICURAZIONI	587	6026	2	3	0.8	23	2.4	4313	266	25394d	3.6c	
8 ALLEANZA ASSICURAZIONI	587	15	-15	-20	6.2	58	1.1	929d	91d	8378d	10.6c	
9 ISTITUTO BANCARIO SAN PAOLO DI TORINO	661	4950	1	0.8	15	2.6	NA	325	124565d	5.6c		
10 ISTITUTO MOBILIARE ITALIANO	671	31	24	1.0	4	4.0	NA	356	44780d	7.6c		
11 RAS	845	4168	11	0	1.3	19	2.1	4452d	211d	18000d	7.1c	
12 BANCA COMMERCIALE ITALIANA	845	2	-9	-14	0.6	4.6	NA	236	102769	4.3		
13 EDISON	859	3721	6	35	27	2.7	21	2.1	659d	2432d	12.4c	
14 MONTEDISON	859	3673	-15	-20	1.2	0.0	15737	691	10947d	23.2c		
15 LUXOTTICA GROUP	910	3450	115	13.5	31	0.7	1194	104	459d	44.2c		
16 BANCA DI ROMA	910	3300	5	0	0.5	58	NA	98309*	0.8*			
17 MEDIOBANCA	910	3257	7	-9	-15	1.3	1.9	NA	129	20416	5.0	

JAPAN

COUNTRY COMPOSITE		2616814	19	8	37	3.0	86	0.7	2930140	23440	9289557	6.2	
1	NIPPON TELEGRAPH & TELEPHONE	3	7271	-10	15	2.9	59	0.6	1973e	11104	4.9c		
2	BANK OF TOKYO-MITSUBISHI	8	110286	24	4	33	4.2	808	0.3	NA	136e	475985	7.1c
3	TOYOTA MOTOR	8	85779	23	18	1.8	36	0.7	99167e	2377e	96169	5.1c	
4	FUJI BANK	8	62988	22	-5	21	3.4	1.1	0.3	NA	-3010e	494257	NEG

	GLOBAL RANK	MARKET VALUE \$ MIL.	PRICE \$	% CHANGE	52-WK HIGH	52-WK LOW	PERF. 1Y	PERF. 3Y	PERF. 5Y	PERF. 10Y	PERF. 15Y	PERF. 20Y		
SUMITOMO BANK	16	61891	20	-5	21	3.5	178	0.4	NA	347e	49318e	1.9c	61	
INDUSTRIAL BANK OF JAPAN	17	60478	26	-12	13	4.0	-103	0.3	NA	377967	NEG	61		
DAI-ICHI KANGYO BANK	21	56294	18	5	22	3.1	77	0.4	NA	500474	4.0c	61		
SANWA BANK	22	55809	19	-10	15	3.0	48	0.3	NA	1156e	481224	NEG	61	
SAKURA BANK	48	37909	11	-9	17	2.2	-23	0.7	NA	1681e	462438	NEG	61	
NOMURA SECURITIES	46	37044	19	5	34	2.3	82	0.5	NA	453e	99994	1.2c	62	
MATSUSHITA ELECTRIC INDUSTRIAL	50	36155	17	11	42	1.2	-69	0.7	62688e	580e	75876	NEG	41	
TOKYO ELECTRIC POWER	55	35790	26	-20	1	2.4	42	1.9	46277	800	126216	5.8	12	
HITACHI LTD.	62	30821	9	-4	22	1.1	23	1.1	76116e	1311e	84566	4.6c	34	
MITSUBISHI HEAVY INDUSTRIES	68	28933	9	25	60	1.7	30	1.0	17910e	9e	37136	8.8c	38	
ASAHI BANK	73	27934	12	-3	24	2.8	-41	0.5	NA	681e	1690e	NEG	61	
TOKAI BANK	78	26964	12	1	37	2.5	-20	0.5	NA	1048e	300331	NEG	61	
SEVEN-ELEVEN JAPAN	80	26357	61	9	16	7.9	52	0.5	13887	488	4101	15.1c	54	
SONY	93	23777	64	32	58	2.5	47	0.7	42461e	502e	39074	5.4c	41	
ITO-YOKADO	96	23448	57	1	37	3.3	33	0.6	26735e	709e	15309	10.0c	54	
HONDA MOTOR	97	23434	24	63	108	2.5	36	0.5	39319e	836e	27885	7.0c	42	
NIPPON STEEL	98	23391	3	-5	21	2.9	46	0.7	27290e	505e	42067	6.3c	25	
SEIBU RAILWAY	101	20888	53	37	75	65.0	440	0.1	6098	-21	11404	NEG	51	
TOSHIBA	102	22363	7	10	41	2.2	37	1.3	47364e	556e	50539	8.1c	34	
KANSAI ELECTRIC POWER	103	22361	23	-12	12	2.0	55	2.0	13611	408	60966	3.7	12	
EAST JAPAN RAILWAY	106	22017	5504	7	36	3.6	35	0.8	22879e	633e	67953e	10.2	51	
MITSUBISHI TRUST & BANKING	109	21686	11	3	31	2.6	-16	0.4	NA	1398e	141769	NEG	62	
MITSUBISHI CORP.	111	21484	14	20	53	2.3	69	0.5	164119e	819e	87879	3.3c	89	
NISSAN MOTOR	118	20006	8	27	63	1.6	35	0.9	56014e	-818e	64639	NEG	41	
TOKIO MARINE & FIRE	127	20070	13	13	44	3.6	77	0.6	11471	260	44576	4.6	63	
LONG-TERM CREDIT BANK OF JAPAN	135	19347	8	-11	13	1.9	-60	0.7	NA	-310e	316489	NEG	61	
DOI	140	18798	6469	30	67	9.9	475	0.1	6194e	43e	7311e	2.1	55	
NIPPONDENSO	141	18751	22	19	52	2.4	41	0.5	18136	461	14274	5.5	37	
SHARP	145	18224	16	16	47	2.3	43	0.7	15044e	428e	18102	5.4c	41	
MITSUBISHI ESTATE	146	18146	14	25	59	3.8	180	0.5	6010	139	23065	2.9	44	
DAIWA SECURITIES	148	18033	13	21	55	2.1	41	0.6	NA	418e	43122	5.1	62	
CHUBU ELECTRIC POWER	165	17307	23	-14	9	2.0	41	2.0	19126	422	54261	4.9	12	
SUMITOMO TRUST & BANKING	168	17265	14	1	29	2.2	-12	0.5	NA	-1472e	139347	NEG	62	
JAPAN TOBACCO	160	17095	6548	-9	16	1.4	27	0.8	32840e	609e	18672	5.3c	43	
NEC	162	17023	11	4	32	2.3	24	0.9	40703e	714e	38403	9.7c	34	
FUJITSU	169	16692	9	-5	21	1.6	29	1.1	34766e	584e	34355	5.7c	33	
CANON	170	16533	20	26	61	2.1	32	0.6	10084	509	20748	6.5	33	
NIKKO SECURITIES	175	16172	11	24	59	2.2	46	0.7	NA	351e	19701	4.8c	62	
FUJI PHOTO FILM	179	15996	31	30	66	1.5	24	0.6	9991e	674e	14777	4.0	46	
ALL NIPPON AIRWAYS	190	14481	11	-5	22	10.9	-224	0.3	8057	-69	10406	NEG	58	
MITSUBISHI ELECTRIC	196	14698	7	-1	26	1.9	27	1.4	32483e	548e	31811	7.0c	34	
TAKEDA CHEMICAL INDUSTRIES	199	14501	17	24	58	2.4	26	0.8	7413e	554e	10275	9.2c	48	
JAPAN AIRLINES	202	14334	8	16	48	5.5	-106	0.0	10474	186	19940	NEG	56	
MIITSUI & CO.	204	14295	9	17	49	2.7	61	0.8	160074e	281e	66160	8.8c	59	
ASAHI GLASS	206	14133	12	-3	24	2.5	62	0.7	10409e	38e	15594e	4.1	36	
DAI NIPPON PRINTING	210	13897	19	11	54	1.9	38	0.8	11610e	494e	10400e	6.8	52	
BRIDGESTONE	212	13857	17	14	52	2.7	37	0.6	10434	801	10449	9.9	37	
MIITSUI TRUST & BANKING	220	13191	11	12	43	2.0	41	0.5	NA	107e	127877	NEG	62	
KIRIN BREWERY	222	13046	12	8	37	2.0	35	0.9	15109	371	13644	5.6	43	
KYOCERA	227	12748	68	-10	16	2.4	17	0.7	8987e	768e	7171	14.0c	34	
KAWASAKI STEEL	244	12032	4	-2	25	2.8	55	0.8	10710e	210e	1096e	5.1c	38	
KINKI NIPPON RAILWAY	246	11975	7	-12	11	6.1	619	0.6	8533	14	18444	1.1	57	
SUMITOMO CORP.	251	11814	11	22	56	1.8	63	0.7	149584e	789e	47381	2.9c	84	
DAIWA BANK	265	11612	7	-26	-5	1.9	-11	0.6	NA	1018e	169488	NEG	61	
SANYO ELECTRIC	268	11406	6	14	48	1.6	-336	0.8	4749e	37e	1181e	NEG	41	
TOHOKU ELECTRIC POWER	263	11444	24	-18	5	2.0	23	2.0	13124	491	10460	5.6	31	
KYUSHU ELECTRIC POWER	264	11415	14	-14	9	2.2	26	1.9	10334	431	38096	8.3	12	
MITSUBISHI CHEMICAL	280	10823	6	3	32	2.4	384	0.6	12397	19	18104	1.0	22	
NIPPON EXPRESS	284	10733	10	18	51	4.4	42	0.6	15810e	257e	9939	1.0c	57	
TOKYO GAS	285	10632	4	-10	16	2.8	104	1.2	8472	102	14677	2.7	11	
SANKYO	289	10616	24	2	31	3.3	29	0.7	5116	362	6195	11.4	41	
ASAHI CHEMICAL INDUSTRY	293	10463	7	3	32	2.7	122	0.8	11190e	8e	11405e	2.2	22	
NINTENDO	294	10432	10	22	50	2.4	19	1.3	3276e	504e	6353	12.9c	46	
SHIZUOKA BANK	295	10421	13	-8	18	2.6	59	0.4	NA	118e	70399	4.4c	61	
NKK	298	10300	3	16	48	2.8	21	0.0	16707e	488e	28878	13.3c	25	
MIITSUI FUDOSAN	299	10296	13	13	44	1.8	122	0.7	11491	84	33762	1.5	64	
ITOCHU	301	10232	7	17	50	2.5	95	0.8	181064e	118e	59504	2.6c	59	
KAJIMA	308	10049	10	6	35	2.8	48	0.8	19359	210	26819	5.8	32	

COUNTRY RANK		GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL	MARKET CAPITALIZATION U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL	PROFITS U.S. \$ MIL	ASSETS U.S. \$ MIL	RETURN ON EQUITY %	INDUS CODE	
73	TOPPAN PRINTING	312	9846	14	5	34	1.9	27	0.8	11008e	367e	9889	7.0c	52
74	OSAKA GAS	314	9846	4	5	34	3.0	-117	1.2	6582	-84	10555	NEG	12
75	BANK OF YOKOHAMA	318	9736	9	8	18	2.1	-16	0.5	NA	-604e	114710	NEG	6
76	SUMITOMO METAL INDUSTRIES	321	9690	3	4	33	2.1	49	0.9	13228e	199e	22405	4.3c	28
77	SUMITOMO ELECTRIC INDUSTRIES	324	9670	14	17	49	2.5	37	0.7	10731e	260e	11107	6.6c	3
78	TONEN	327	9570	15	-13	11	3.3	51	2.5	5430	186	6456	6.4	1
79	KOMATSU	328	9566	10	22	56	1.8	72	0.8	9244e	132e	14264	2.5c	38
80	TORAY INDUSTRIES	330	9464	7	4	33	2.2	56	1.0	8708e	169e	11464	4.0c	22
81	KUBOTA	332	9415	7	-3	24	3.2	40	0.8	9914e	238e	11672	8.0c	3
82	FANUC	335	9343	39	-10	15	2.2	39	0.5	1570e	240e	4793	5.7c	3
83	JUSCO	338	9275	30	36	74	3.7	32	0.6	18585e	288e	11725	11.8c	5
84	SHIMIZU	344	9045	11	13	44	2.8	-249	0.7	19262	-36	25131	NEG	3
85	MURATA MFG.	355	8747	37	-4	23	2.3	25	0.4	2977e	345e	5150	9.0c	3
86	YAMAICHI SECURITIES	357	8721	7	20	53	1.5	-13	0.6	NA	-654	33885	NEG	6
87	DAIEI	358	8715	12	-2	26	6.6	185	1.3	29232e	47e	19781e	3.5	5
88	JAPAN TELECOM	359	8694	20999	6	36	3.1	44	0.3	3104e*	197e*	4484*	7.1c*	5
89	CHUGOKU ELECTRIC POWER	366	8375	23	-12	13	2.0	32	2.0	9606	265	24212	6.4	1
90	SEKISUI HOUSE	371	8282	12	-7	19	1.2	22	1.4	12118e	379e	15137	5.7c	3
91	TOKYU CORP.	376	8220	7	16	48	3.7	470	0.6	4345	17	14523	0.8	5
92	MARUBENI	380	8138	5	2	31	1.8	58	1.0	143848e	140e	63312	3.1c	5
93	NIPPON OIL	381	8125	7	2	30	1.4	53	1.0	23867e	153e	24425	2.6c	1
94	SUMITOMO CHEMICAL	383	8101	5	2	25	3.6	47	0.6	8806e	171e	12454	7.5c	2
95	MATSUSHITA ELECTRIC WORKS	387	8034	11	-8	17	1.7	34	1.1	10374	233	11614	5.1	2
96	KAO	392	8006	13	11	41	2.5	35	0.9	7730e	227e	6561	7.2c	4
97	KOBE STEEL	400	7816	3	-2	26	3.2	9	0.0	13663e	835e	22112	34.1c	2
98	AJINOMOTO	401	7804	12	6	35	2.3	80	0.8	6946e	97e	7055	2.9c	4
99	NTT DATA COMMUNICATIONS SYSTEMS	403	7794	30805	101	156	13.5	72	0.2	5201e	108e	6697	18.7c	5
100	MITSUBISHI MOTORS	406	7724	8	-3	24	1.7	66	0.8	32720e	118e	26147	2.7c	4
101	TAISEI	408	7688	8	17	50	2.1	51	0.9	18485	151	29532	4.1	3
102	DAIWA HOUSE INDUSTRY	410	7635	15	-2	25	1.7	21	1.0	9071	354	10106	8.4	3
103	TAISHO PHARMACEUTICAL	411	7635	22	19	52	2.9	26	0.8	2044e*	296e*	3429*	11.3c*	4
104	MARUI	415	7564	21	38	76	2.1	44	1.0	4855e	171e	6679	4.7c	5
105	TOYO TRUST & BANKING	420	7489	10	2	30	1.7	-10	0.5	NA	-723e	75175	NEG	6
106	TDK	422	7485	57	26	61	2.2	29	0.8	5009e	256e	5211	7.5c	5
107	SECOM	426	7412	65	3	31	3.4	42	0.7	2395	174	3716	8.1	5
108	TOYO SEIKAN KAISHA	440	7203	36	8	38	2.0	25	0.2	7208	290	6362	8.0	2
109	ROHM	441	7181	63	37	75	3.1	20	0.3	2704e	353e	3713	15.3c	3
110	KAWASAKI HEAVY INDUSTRIES	443	7060	5	39	78	5.0	46	1.0	10049e	152e	11024	10.8c	3
111	YAMANOUCHI PHARMACEUTICAL	448	6973	22	-3	23	1.8	19	0.8	3831e	375e	7357	9.9c	4
112	NIPPON YUSEN	453	6890	6	-2	26	3.3	236	0.6	8027	29	12613	1.4	5
113	OBAYASHI	454	6852	9	21	54	2.6	101	0.8	13154	68	21525	2.5	3
114	SHIN-ETSU CHEMICAL	460	6794	20	16	49	2.6	19	0.3	5321e	350e	5957	13.3c	2
115	CHIBA BANK	461	6757	9	-13	10	1.9	144	0.5	NA	47e*	82199e*	1.3*	6
116	YASUDA TRUST & BANKING	467	6675	6	-18	4	1.3	-7	0.8	NA	-890e	88062	NEG	6
117	MITSUBISHI MATERIALS	470	6610	6	20	54	2.5	-191	0.8	10650	-35	13722	NEG	2
118	YASUDA FIRE & MARINE	471	6605	7	10	40	2.9	66	0.9	8151	99	32750	4.4	6
119	RICOH	474	6593	10	26	60	1.9	33	0.9	10268e	202e	12217	5.8c	3
120	SEKISUI CHEMICAL	478	6535	12	1	29	1.8	311	0.9	9463	21	7918	0.6	2
121	NIPPON CREDIT BANK	481	6486	4	-32	-13	1.2	-9	1.4	NA	-707e	161420	NEG	6
122	NEW OJI PAPER	483	6482	9	-16	7	2.0	43	1.0	7630e	149e	9084	4.7c	2
123	SHIKOKU ELECTRIC POWER	490	6401	23	-12	12	2.0	45	2.0	5117	143	13483	4.5	1
124	TOSTEM	491	6396	29	-13	10	2.1	27	0.6	5141	236	5378	7.8	2
125	NIPPON PAPER INDUSTRIES	495	6362	7	-10	15	2.4	142	1.1	9151	45	10571	1.7	2
126	HACHIJUNI BANK	496	6360	11	-14	10	2.7	130	0.4	NA	49e*	50145*	2.1c*	6
127	JOYO BANK	501	6308	8	11	13	2.1	130	0.6	NA	48e*	70027*	1.6c*	6
128	ACOM	530	6036	41	NA	NA	2.9	21	0.7	NA	292e*	10344e*	14.2*	6
129	SUMITOMO MARINE & FIRE	533	6021	9	7	36	2.7	64	0.8	4823	93	22751	4.2	6
130	KDD	535	6005	93	7	37	1.9	47	0.5	2656e	127e	5414	4.1c	5
131	ISHIKAWAJIMA-HARIMA HEAVY INDUSTRIES	544	5958	5	16	48	3.4	33	1.2	10083e	181e	12556	10.4c	3
132	MAZDA MOTOR	552	5823	5	33	69	1.7	-53	0.0	17021e	-110e	13188	NEG	4
133	TOYODA AUTOMATIC LOOM WORKS	563	5689	20	15	46	2.4	45	0.6	4619e	125e	3952	5.3c	3
134	SUZUKI MOTOR	564	5686	13	27	62	2.1	31	0.5	11640	186	8102	6.8	4
135	GUNMA BANK	565	5683	11	-6	20	2.7	120	0.4	NA	48e*	49453*	2.2c*	6
136	MITSUI MARINE & FIRE	577	5610	8	11	41	2.7	68	0.9	5733e	83e	23880	4.0c	6
137	ISUZU MOTORS	578	5607	5	33	70	8.1	39	0.8	7016g	60g	13368	20.7	3
138	TOBU RAILWAY	583	5568	6	4	32	4.1	514	0.7	3202	11	10310	0.8	5
139	HITACHI ZOSEN	585	5553	6	29	65	6.0	67	1.0	5531e	83e	6174	9.0c	3
140	SONY MUSIC ENTERTAINMENT	598	5454	50	23	57	2.7	59	0.6	1821e	93e	2536	4.6c	4
141	OMRON	618	5310	20	9	39	2.0	39	0.6	4859e	135e	5265	5.1c	3
142	SUMITOMO METAL MINING	620	5298	9	18	51	2.7	435	0.6	4300	12	5471	0.6	2
143	MITSUKOSHI	621	5295	11	33	70	7.2	-223	0.5	9418e	24e	5673e	NEG	6
144	HANKYU CORP.	642	5114	6	-1	27	3.6	-42	0.0	3368	-121	11177	NEG	5



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THE BUSINESS WEEK GLOBAL 1000

COUNTRY RANK	GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUS. CODE		
145	HOKURIKU ELECTRIC POWER	648	5055	23	-10	14	1.9	36	2.0	4360	140	13383	5.2	12
146	TEIJIN	650	5039	5	2	30	1.7	64	1.1	5723e	79e	8320	2.7c	22
147	HOKKAIDO ELECTRIC POWER	655	4993	23	-11	14	2.1	23	2.0	5031	217	12361	9.1	17
148	EISAI	657	4972	18	9	40	2.4	28	0.8	2529e	176e	4097e	8.4	43
149	TOTO	658	4969	15	-4	22	2.2	46	0.7	4204e	108e	4061	4.8c	27
150	PROMISE	659	4967	50	NA	NA	2.6	17	1.0	1866e	291e	8801e	15.2	62
151	SHISEIDO	660	4961	12	2	30	1.5	31	0.9	5188e	162e	5221	5.1c	44
152	ASAHI BREWERIES	663	4946	12	-2	25	1.8	82	0.7	10083	61	15984	2.2	43
153	BANK OF FUKUOKA	667	4918	8	-2	26	2.1	-28	0.6	NA	-174e*	58333*	NEG	61
154	ODAKYU ELECTRIC RAILWAY	672	4892	7	-10	14	3.8	174	0.7	5212	28	9592	2.2	52
155	MATSUSHITA COMMUNICATION INDUSTRIAL	678	4838	26	24	58	2.5	73	0.5	5507e	66e	3340	3.5c	33
156	SMC	685	4767	79	47	88	4.7	32	0.1	1371e	149e	2242	14.6c	38
157	SEGA ENTERPRISES	694	4720	47	25	60	3.3	121	0.8	3560e	39e	4343	2.7c	44
158	TOKYO ELECTRON	708	4612	31	-4	22	3.3	51	0.7	2328	90	2944	6.3	38
159	TAKASHIMAYA	710	4597	16	20	53	3.3	25	0.4	11101e	184e	8128	13.2c	54
160	NIKON	719	4517	12	32	69	3.7	318	0.5	2669	14	3436	1.2	39
161	KEYENCE	720	4508	131	NA	NA	4.7	62	0.1	358	72	1038	7.5	39
162	NISSHO IWAI	728	4441	6	30	66	2.0	-19	0.8	87419e	-232e	45323	NEG	59
163	YAMATO TRANSPORT	733	4408	12	8	37	2.5	38	0.9	6064e	117e	4339	6.6c	57
164	KYOWA HAKKO KOGYO	737	4377	10	-2	25	3.0	30	0.7	3469	144	3783d	9.8c	42
165	YAMAZAKI BAKING	740	4361	20	-1	27	2.3	35	0.6	5977	126	3795	6.6	44
166	EBARA	741	4359	15	8	38	3.8	59	0.6	4542e	74e	4558	6.4c	38
167	NICHII	742	4359	16	39	77	2.2	466	1.2	15634e	9e	13426	0.5c	54
168	ONO PHARMACEUTICAL	750	4287	35	-27	-7	2.9	18	0.7	1220e*	234e*	2270*	15.7c*	43
169	NSK	755	4264	8	28	64	2.0	107	0.7	3846	40	6192	1.9	39
170	KINDEN	757	4256	16	-10	15	1.8	23	0.6	5198e*	188e*	5610e*	7.8*	39
171	AININ SEIKI	758	4255	15	40	78	1.9	31	0.7	7664e	139e	5784	6.1c	39
172	HOKURIKU BANK	759	4252	6	-15	8	1.4	-15	0.6	NA	-277e	72881	NEG	61
173	OKI ELECTRIC INDUSTRY	763	4242	7	10	41	2.4	19	0.9	6923e	228e	6836	12.9c	39
174	JAPAN ENERGY	767	4220	4	7	37	3.6	-28	1.2	17299	-153	14774	NEG	13
175	DAIICHI PHARMACEUTICAL	771	4201	15	1	28	1.9	21	0.9	2421e	198e	4266	8.8c	43
176	NAGOYA RAILROAD	779	4145	5	-2	25	2.9	1325	0.8	3485	3	9616	0.2	52
177	COSMO OIL	781	4108	7	4	33	2.4	68	1.1	14396e	61e	11896e	3.5	11
178	NISSHIN STEEL	782	4100	4	-7	19	1.8	30	1.1	4212e	139e	6162	5.9c	23
179	FAMILYMART	790	4049	46	3	32	5.4	39	0.5	4129d	80d	1425	13.9c	59
180	HITACHI METALS	795	4031	11	-2	25	2.4	22	0.8	4337e	184e	4642	10.9c	7
181	ASHIKAGA BANK	801	3993	6	-15	8	2.5	-5	0.4	NA	-850e*	61037e*	NEG	61
182	UNY	802	3993	21	33	70	2.4	35	0.7	8430e	114e	4797	6.8c	59
183	PIONEER ELECTRONIC	803	3987	22	28	63	1.5	-43	0.4	4686e	-92e	4392	NEG	44
184	SHOWA SHELL SEKIYU	805	3974	11	4	33	2.4	31	0.8	13332	128	8184d	7.6c	1
185	BENESSE	806	3967	87	NA	NA	3.7	42	0.1	1922e	94e	2395e	8.7	59
186	NGK INSULATORS	809	3946	11	19	52	2.6	46	0.7	2171e	86e	3187	5.6c	39
187	FUJI ELECTRIC	811	3936	6	10	41	2.4	72	1.3	8237e	54e	7648	3.3c	39
188	MATSUSHITA-KOTOBUKI ELECTRONICS INDUSTRIES	812	3935	25	29	65	2.4	63	0.5	4414e	62e	2672	3.7c	49
189	MITSUBISHI OIL	817	3907	9	11	14	1.9	43	1.1	10361e	92e	8550	4.4c	1
190	DAINIPPON INK & CHEMICALS	825	3873	5	2	31	2.2	65	1.1	7860	59	9836	3.3	2
191	KEIO TEITO ELECTRIC RAILWAY	826	3872	6	-4	23	3.1	85	0.8	4165	45	5595	3.7	5
192	FURUKAWA ELECTRIC	828	3861	6	16	48	2.1	63	0.9	6506e	61e	7573	3.4c	3
193	NIPPON FIRE & MARINE	834	3835	7	5	33	2.0	56	1.0	4001e*	65e*	17807*	3.6c*	61
194	KOKUSAI SECURITIES	836	3833	15	NA	NA	1.9	89	0.6	NA	43e	6509	2.1c	61
195	NICHIEI	837	3826	68	NA	NA	4.0	21	0.7	930e	181e	4058e	18.9	6
196	mitsui O. S.K. LINES	842	3799	3	16	48	3.4	-92	0.0	5877	41	9438	NEG	5
197	HOYA	848	3728	32	13	44	3.3	36	0.6	1546e	102e	1776	9.0c	44
198	AUTOBACS SEVEN	856	3699	97	NA	NA	4.1	37	0.2	1675	77	1351	10.9	39
199	NICHIDO FIRE & MARINE	862	3655	8	5	34	2.3	53	0.8	3696e*	70e*	15232*	4.4c*	61
200	KURARAY	863	3652	11	3	31	2.3	36	0.7	3061e	102e	4421	6.5c	2
201	77 BANK	865	3646	10	-12	12	2.3	36	0.5	NA	102e*	41326*	6.5c*	61
202	VICTOR CO. OF JAPAN	873	3621	14	32	68	1.6	662	0.0	7097	5	4817	0.2	4
203	ADVANTEST	876	3616	44	40	78	3.2	20	0.4	1354e	184e	1775e	16.3	3
204	NIPPON TELEVISION NETWORK	882	3587	283	27	62	2.9	54	0.4	2233	67	1887	5.5	5
205	HIROSHIMA BANK	883	3581	6	-4	22	1.7	-9	0.8	NA	-398e*	59539*	NEG	61
206	CHUGOKU BANK	898	3521	17	-7	18	1.6	141	0.3	NA	25e*	44498e*	1.2*	61
207	KOKUYO	902	3495	27	9	40	2.3	42	0.5	2767	83	2564	5.6	59
208	CHICHIBU ONODA CEMENT	905	3464	6	20	53	2.0	-62	0.8	4886	-56	7815	NEG	2
209	NISSIN FOOD PRODUCTS	906	3461	26	6	36	2.0	49	0.9	2553e	70e	2573	4.1c	44
210	FUJISAWA PHARMACEUTICAL	915	3416	11	-15	8	1.6	69	0.7	2627	50	4746	2.4	4
211	YAMAGUCHI BANK	921	3404	17	-15	8	1.8	116	0.3	NA	29e*	41356*	1.6c*	61
212	CANON SALES	924	3396	27	9	40	1.8	53	0.5	6330	64	4598	3.4	5
213	BANYU PHARMACEUTICAL	927	3395	13	14	45	2.0	34	0.7	1210e*	101e*	2130e*	6.0*	49
214	SHOWA DENKO	932	3342	3	-1	27	3.9	-1881	0.0	4998	-2	6908d	NEG	2
215	GENERAL SEKIYU	933	3341	9	-18	4	2.9	28	2.6	4810e	121e	3373	10.5c	17
216	NIPPON MEAT PACKERS	939	3330	15	0	27	1.8	34	1.0	6994	98	4991	5.2	4



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THE BUSINESS WEEK GLOBAL 1000

COUNTRY RANK		GLOBAL 1000 RANK	MARKET CAPITAL \$ MIL	PER SHARE U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL	PROFITS U.S. \$ MIL	ASSETS U.S. \$ MIL	RETURN ON EQUITY %	INDUS COT	
217	NTN	961	3290	7	21	54	2.2	109	1.2	2792	30	4071	2.0	3
218	HINO MOTORS	963	3262	9	17	50	2.7	65	0.6	6021	50	3717	4.2	3
219	CREDIT SAISON	966	3259	24	11	42	2.5	32	0.4	NA	96e*	7386e*	7.9*	6
220	MITSUI TOATSU CHEMICALS	971	3246	4	7	36	2.3	7483	0.7	4583	0	7109	0.0	2
221	MINEBEA	975	3234	8	28	63	3.1	48	0.8	2410e	68e	4902	6.5c	3
222	TOKYO STEEL MFG.	976	3234	21	19	51	1.9	-36	0.3	1349e*	-91e*	2506*	NEG	2
223	SAPPORO BREWERIES	982	3226	10	7	19	2.5	145	0.7	6130	22	8585e	1.7c	4
224	TODA	986	3214	10	-1	27	2.1	51	0.8	5786e*	63e*	7667e*	4.1*	3
225	SUMITOMO REALTY & DEVELOPMENT	988	3210	8	28	63	1.4	646	0.7	2732	5	17445	0.2	6
226	HITACHI CABLE	991	3200	9	11	41	2.0	37	1.0	3537e	87e	3304	5.4c	3
227	NISSHIN FLOUR MILLING	995	3186	13	15	47	2.4	55	0.4	3212e	58e	2346	4.3c	4

NETHERLANDS

COUNTRY COMPOSITE			264095	93	28	39	3.5	21	2.4	268877	19973	1042391	22.3	
1	ROYAL DUTCH PETROLEUM (1)	NR	81146	151	21	31	2.4	18	3.7	107830	6779	117700	13.6	1
2	ING GROEP	91	24035	82	52	64	1.7	15	3.0	NA	1521	231503	12.0	6
3	UNILEVER NV (2)	NR	21729	136	8	17	4.7	18	2.7	49814	2328	30118	26.7	4
4	ABN AMRO HOLDING	154	17340	55	46	58	1.6	12	3.8	NA	1383	319288	12.8	6
5	KONINKLIJKE PTT NEDERLAND	167	16716	36	0	8	2.0	13	4.2	11190	1202	16884	15.4	5
6	AEGON	236	12542	48	48	60	2.6	16	2.9	8043	773	87984	16.6	6
7	PHILIPS ELECTRONICS	241	12216	35	11	4	1.5	8	2.6	37660	1568	30521	17.9	4
8	HEINEKEN	265	11353	226	59	72	4.1	29	0.9	6101	388	5632	14.0	4
9	POLYGRAM	291	10516	58	0	8	6.6	24	0.9	5140	433	4791	27.1	4
10	ELSEVIER (5)	NR	10263	15	34	45	6.8	25	2.2	5654	855	8520	27.2	5
11	AKZO NOBEL	361	8583	121	-1	7	2.2	12	3.4	12554	741	10856	18.7	2
12	WOLTERS KLUWER	401	7487	112	33	44	17.4	29	1.1	1720	258	1181	60.1	5
13	KONINKLIJKE AHOLD	468	6668	54	55	68	5.1	25	1.6	17303	267	5401	20.4	5
14	FORTIS AMEV (6)	NR	5637	78	43	55	1.7	13	3.2	NA	808	160623	12.5	6
15	DORDTSCH PETROLEUM	581	5602	160	19	29	19.2	31	3.3	NA	179	293	61.6	1
16	HEINEKEN HOLDING	644	5093	203	57	70	3.7	36	1.0	NA	143	1412	10.3	4
17	GUCCI GROUP	813	3930	67	NA	NA	-21.2	48	0.4	500e	81e	198	NA	4
18	KLM ROYAL DUTCH AIRLINES	973	3238	36	14	23	1.6	13	2.5	5368	266	9486	12.2	5

NEW ZEALAND

COUNTRY COMPOSITE		11451	3	-6	-8	3.3	14	4.5	4254	795	8214	22.0		
1	TELECOM CORP. OF NEW ZEALAND	409	7678	4	2	0	5.4	16	5.9	2165e	487e	3100	34.4c	5
2	CARTER HOLT HARVEY	843	3773	2	-13	-15	1.2	12	3.1	2089e	308e	5114	9.6c	2

NORWAY

COUNTRY COMPOSITE			10854	47	15	20	2.2	10	1.9	12207	1091	13605	21.9
1	NORSK HYDRO	278	10854	47	15	20	2.2	10	1.9	12207	1091	13605	21.9

SINGAPORE

COUNTRY COMPOSITE		123284	9	6	7	3.3	23	1.7	22111	4908	174367	12.8	
1	SINGAPORE TELECOMMUNICATIONS	34	42623	3	37	38	14.0	43	0.6	2494	940	4819	32.3
2	SINGAPORE AIRLINES	219	13192	10	8	9	1.9	18	1.2	4887e	727e	9360e	10.5
3	OCBC OVERSEAS CHINESE BANK	256	11608	13	4	5	3.2	27	0.6	NA	429	32254	11.9
4	UNITED OVERSEAS BANK	372	8279	9	-9	-8	3.3	18	1.0	NA	449	26496d	17.7c
5	DEVELOPMENT BANK OF SINGAPORE	386	8050	12	1	2	2.0	19	0.7	NA	422	34891	10.8
6	SINGAPORE PRESS HOLDINGS	400	6335	19	20	20	5.3	28	0.8	591	221	1414	19.1
7	CITY DEVELOPMENTS	529	6037	8	15	16	4.0	21	0.5	NA	284	5058	18.8
8	HONGKONG LAND HOLDINGS	545	5954	2	6	6	0.8	23	5.2	NA	257	9617	3.4
9	JARDINE MATHESON HOLDINGS	571	5635	8	-2	-2	1.7	13	3.2	10636	420	11583	12.8
10	OVERSEAS UNION BANK	679	4823	7	11	12	2.3	26	0.9	NA	184	18179	8.8
11	KEPPEL	739	4370	8	-8	-7	2.2	28	0.8	1706	152	9479d	7.9c
12	FRASER & NEAVE	992	3195	11	9	10	1.5	34	1.1	1797	131	3177	6.5
13	JARDINE STRATEGIC HOLDINGS	996	3185	3	-14	14	0.7	11	4.8	NA	292	8040	6.6

SPAIN

COUNTRY COMPOSITE		96702	54	23	29	2.4	17	3.4	51495	6569	568415	15.1
1 TELEFONICA NACIONAL DE ESPANA	166	16833	18	37	43	1.4	16	3.3	13501	1033	37373	9.1
2 ENDESA	178	16033	62	29	36	2.7	13	2.3	6856	1162	16045d	20.5c
3 REPSOL	200	10239	14	6	11	2.3	11	3.3	18377g	751d	12462d	21.3c
4 IBERDROLA	331	9399	10	-45	52	1.2	14	4.0	6276	659	24416d	9.7c
5 BANCO BILBAO VIZCAYA	364	8480	38	31	37	1.7	13	4.1	NA	652	101235d	13.6c
6 BANCO DE SANTANDER	435	7272	46	21	27	1.6	12	4.8	NA	585	127677	13.3
7 GAS NATURAL SDG	475	6570	176	62	71	5.5	21	0.8	2250	278	4094d	25.9c
8 ARGENTARIA, CORP. BANCARIA DE ESPANA	628	5247	42	19	25	1.1	9	5.0	NA	576	90440d	13.0c
9 BANCO POPULAR ESPANOL	651	5032	174	16	22	2.1	11	4.2	NA	446	25948	19.1
10 PRYCA	709	4111	23	27	34	1.1	15	1.5	4215	369	2404d	20.4c
11 BANESTO	824	3873	6	9	4	2.6	22	0.0	NA	161	39325	11.9
12 BANCO CENTRAL	953	3285	10	-10	-8	1.0	33	5.8	NA	97	86996	3.1

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As of March 31, 1996

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<i>Average International Small Company Fund</i>	<i>18.4%</i>	<i>3.2%</i> (3-31-94; 3-31-96)
Twentieth Century International Equity Fund	18.4%	12.7% (5/9/91)
<i>EAFE (Europe, Australia, Far East) Index**</i>	<i>12.3%</i>	<i>8.4%</i> (4-30-91; 3-31-96)
<i>Average International Fund†</i>	<i>16.1%</i>	<i>9.5%</i> (3-30-91; 3-31-96)

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COUNTRY RANK	GLOBAL 1000 RANK	MARKET VALUE \$ MIL	PRICE PER SHARE U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL	PROFITS U.S. \$ MIL	ASSETS U.S. \$ MIL	RETURN ON EQUITY %	INDUSTRY CODE
SWEDEN												
COUNTRY COMPOSITE		133204	30	32	21	2.5	11	3.1	139872	11621	404905	26.5
1 ASTRA	70	28088	46	56	43	6.6	21	1.0	5320	1302	6496	31.2 45
2 L. M. ERICSSON	112	21415	22	30	20	4.4	26	1.2	14678	808	13497	17.3 34
3 VOLVO	315	9826	21	37	26	1.5	8	NA	24384	1263	19495	18.8 42
4 ABB AB (4)	NR	9642	103	22	12	4.0	14	2.3	33/38	1315	32076	29.4 34
5 SANDVIK	516	6166	22	26	16	2.5	11	4.0	4413	554	4541	21.8 25
6 INVESTOR	566	5615	37	48	36	2.7	3	3.7	NA	447	13838	104.7 71
7 SCANIA	569	5647	28	NA	NA	5.4	12	2.9	5177	487	4263	44.9 38
8 SVENSKA HANDELSBANKEN	701	4675	21	46	34	1.3	7	2.7	NA	629	70777	17.8 61
9 STORA KOPPARBERGS BERGSLAGS	754	4267	13	6	-3	1.0	6	4.2	8486	797	9154	17.8 23
10 SKANDINAVISKA ENSKILDA BANKEN	777	4150	8	42	30	1.2	9	2.8	NA	376	65199	13.7 61
11 SKANSKA	783	4098	33	44	32	2.9	16	2.3	5737	257	6261d	18.0c 32
12 AGA	797	4014	16	39	28	3.0	9	2.4	1972	314	3092	35.1 22
13 SYDKRAFT	814	3930	22	41	29	2.0	15	2.6	1806	262	5827	13.2 12
14 SVENSKA CELLULOSA AKTIEBOLAGET	829	3857	20	8	-1	1.2	8	3.6	9706	515	10124	14.8 23
15 NORDBANKEN	832	3850	18	NA	NA	1.5	5	6.2	NA	763	50389	31.6 61
16 ELECTROLUX	847	3733	51	10	1	1.2	9	3.6	17207	408	12356	13.1 41
17 INCENTIVE	900	3505	51	36	25	2.0	9	2.6	3614	361	4779	22.1 45
18 ATLAS COPCO	918	3413	19	27	17	2.3	12	2.4	3634	271	3296	19.7 38
19 SPARBANKEN SVERIGE	958	3266	12	NA	NA	1.1	6	4.4	NA	492	69445	18.0 61

SWITZERLAND

COUNTRY COMPOSITE		318312	1696	18	26	3.0	19	1.8	166927	16541	1215611	15.2
1 ROCHE HOLDING	11	73313	12158	13	21	7.7	39	0.4	11756	2693	28400	19.8 45
2 NESTLE	31	44052	1126	12	20	3.5	19	1.9	45106	2330	36117d	18.4c 44
3 SANDOZ	42	39262	1040	52	63	6.2	24	1.2	12173	1645	16305	26.1 45
4 CIBA-GEIGY	59	31862	1096	54	65	2.4	18	1.5	16529	1722	23933	13.1 22
5 UNION BANK OF SWITZERLAND	87	24329	936	-7	-1	1.3	18	2.7	NA	1336	308871	7.3 61
6 CS HOLDING	172	16268	86	-8	-1	1.6	15	3.7	NA	1119	329586	10.7 61
7 SWISS RE	216	13565	965	28	37	2.2	16	1.9	9699d	744d	33938d	14.4c 63
8 SWISS BANK CORP.	217	13502	178	-1	7	1.3	16	3.6	NA	841	230206	7.9 61
9 ZURICH INSURANCE GROUP	245	11992	264	13	21	1.6	17	1.8	1895	698	73068d	9.1c 63
10 ABB AG (4)	NR	10879	1195	17	26	4.1	16	2.0	33738	1315	32076	25.2 34
11 COMPAGNIE FINANCIERE RICHEMONT	362	8506	1481	30	39	3.6	18	0.7	5968	406	4966	19.6 71
12 HOLDERBANK FINANCIERE GLARUS	597	5459	767	-3	4	1.5	15	1.8	NA	370	11538	10.5 21
13 WINTERTHUR	637	5175	589	-5	2	1.3	15	2.6	15900	324	64873	8.8 63
14 S.M.H.	682	4800	683	20	29	2.7	21	1.0	2105	218	2539d	12.9c 46
15 ALUSUISSE-LONZA HOLDING	683	4794	781	33	42	3.3	16	1.9	5981	307	4910	21.3 71
16 SGS STE GENERALE DE SURVEILLANCE HOLDING	815	3926	2252	25	34	4.8	22	2.0	2099	183	2073	21.7 52
17 PHARMA VISION 2000	925	3395	4552	19	28	2.5	NA	0.0	NA	149*	1823*	NA 62
18 ELEKTROWATT	977	3233	377	30	40	2.5	23	2.4	3978	141	10389	11.0 12

UNITED STATES

COUNTRY COMPOSITE		5108144	125	42	42	5.0	28	2.0	3494652	276442	9022818	21.2
1 GENERAL ELECTRIC	1	137345	83	43	43	4.7	21	2.2	70028	6573	228035	22.5 34
2 COCA-COLA	4	115070	46	49	49	21.4	38	1.1	18018	2986	15041	56.7 43
3 EXXON	6	105266	85	19	19	2.6	16	3.7	107893	6470	91296	16.6 11
4 AT&T	7	99721	62	23	23	5.8	18	2.1	79609	5519	88884	32.7 55
5 PHILIP MORRIS	9	82087	99	36	36	5.9	15	4.0	53139	5478	53811	40.4 43
6 MERCK	10	78619	65	38	38	6.8	23	2.1	16681	3335	23832	29.2 45
7 MICROSOFT	12	71642	119	40	40	13.1	38	0.0	5937	1453	7210	34.6 52
8 JOHNSON & JOHNSON	13	64877	97	47	47	7.0	25	1.6	18842	2403	17873	27.9 45
9 INTEL	15	62091	76	35	35	5.1	19	0.3	16202	3566	17504	27.3 35
10 PROCTER & GAMBLE	18	60276	88	22	22	7.0	21	1.8	33434	2645	28125	33.0 44
11 WAL-MART STORES	19	59346	26	4	4	4.0	22	0.8	93627e	2740e	37541e	18.6 54
12 INTERNATIONAL BUSINESS MACHINES	20	57610	107	15	15	2.6	10	1.3	71940	6018	80292	26.8 33
13 HEWLETT-PACKARD	23	54304	107	61	61	4.6	20	0.9	31519	2433	24427	22.6 33
14 PEPSICO	24	52434	33	36	36	7.2	32	1.4	30421	1606	25432	22.5 43
15 PFIZER	27	45283	71	61	61	8.2	27	1.7	10021	1554	17229	30.1 45
16 DUPONT	28	44698	80	17	17	5.4	14	2.9	36508	3293	37312	38.5 22
17 AMERICAN INTERNATIONAL GROUP (7)	29	44692	94	24	24	2.3	17	0.4	25792	2510	134136	13.2 63
18 MOBIL	30	44512	113	13	13	2.6	15	3.5	64713	2846	42138	16.8 11
19 BRISTOL-MYERS SQUIBB	32	42988	85	29	29	7.4	16	3.5	13767	2600	13929	45.9 45
20 FORD MOTOR	33	42872	37	25	25	1.7	14	3.8	137137	4139	243283	12.7 42
21 WALT DISNEY	35	42175	61	9	9	2.8	33	0.7	18908	988	33225	8.5 53
22 GENERAL MOTORS	36	41684	55	15	15	1.8	8	2.9	168829	6718	217123	21.8 42
23 GTE	37	41629	43	28	28	6.1	16	4.4	19957	2538	37019	38.2 55
24 BELLSOUTH	38	40377	41	33	33	3.4	25	3.5	17886	1564	31880	13.9 55

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THE BUSINESS WEEK GLOBAL 1000

COUNTRY RANK	COMPANY RANK	PER SHARE U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE		
25	CITICORP	40307	84	57	57	2.2	11	2.1	NA	3464	256853	18.9	61
26	MOTOROLA	39117	67	11	11	3.6	23	0.7	27037	1781	22801	15.8	35
27	CHEVRON	38996	60	22	22	2.7	18	3.3	31322	1962	34330	15.2	11
28	BERKSHIRE HATHAWAY (7)	36417	30500	34	34	2.1	16	0.0	4471	725	29929	13.2	71
29	AMOCO	35998	73	6	6	2.4	15	3.6	27066	2159	29845	15.7	11
30	ELI LILLY	35500	64	72	72	6.5	27	2.1	6764	1307	14413	23.9	45
31	ABBOTT LABORATORIES	33899	43	8	8	7.7	20	2.2	10012	1689	9413	39.5	45
32	AMERICAN HOME PRODUCTS	33725	54	45	45	6.1	21	2.9	13376	1482	21363	28.5	45
33	FANNIE MAE	33716	31	33	33	3.1	15	2.5	NA	2156	316550	20.4	62
34	MCDONALD'S	33651	48	27	27	4.5	24	0.6	9795	1427	15415	18.8	53
35	AMERITECH	31308	57	27	27	4.5	15	3.8	13428	1966	21943	28.8	55
36	CISCO SYSTEMS	30490	55	150	150	21.6	43	0.0	1979	421	1757	50.6	33
37	CHASE MANHATTAN	30467	70	52	52	1.7	10	3.2	NA	2970	303989	16.4	61
38	SBC COMMUNICATIONS	30077	49	10	10	4.8	15	3.5	12670	1889	22003	31.3	55
39	BOEING	29365	85	45	45	3.0	40	1.3	19515	783	22098	7.3	31
40	MINNESOTA MINING & MFG.	28572	68	14	14	4.2	22	2.8	13460	1306	14183	19.1	71
41	BANKAMERICA	27535	75	44	44	1.6	11	2.9	NA	2664	232446	14.2	61
42	BELL ATLANTIC	27309	62	12	12	4.1	16	4.6	13430	1639	24157	26.2	55
43	ELECTRONIC DATA SYSTEMS (7)	27269	56	33	33	5.5	28	1.1	12422	939	10832	19.3	52
44	GILLETTE	26308	59	40	40	10.9	31	1.2	6795	824	6340	35.3	45
45	EASTMAN KODAK	25257	74	23	23	5.0	20	2.2	14980	1252	14477	25.0	46
46	CHRYSLER	24917	67	53	53	2.3	10	4.2	53195	2121	53756	22.1	42
47	HOME DEPOT	24483	51	23	23	4.9	32	0.4	15470e	732e	7354e	15.4	54
48	NATIONSBANK	24295	81	43	43	1.8	11	2.9	NA	1950	187298	16.2	61
49	HUGHES ELECTRONICS (7)	24294	61	49	49	2.9	22	1.6	14714	1108	15974	13.0	31
50	LUCENT TECHNOLOGIES	24193	38	NA	NA	12.5	27	0.8	21413	962	21222	45.7	34
51	COLUMBIA/HCA HEALTHCARE	23983	54	32	32	3.4	20	0.2	17695	1299	19892	17.0	52
52	WELLS FARGO	23112	41	31	31	1.6	16	2.2	NA	1549	116061	10.0	61
53	ORACLE	22210	33	43	43	17.8	43	0.0	2967	442	2425	41.5	52
54	TEXACO	22126	84	22	22	2.5	15	3.8	36787	1367	24937	17.1	11
55	AMERICAN EXPRESS	21946	46	29	29	2.8	14	2.0	NA	1564	107405	19.3	62
56	SCHERING-PLOUGH	21909	59	49	49	13.1	20	2.3	5104	1053	4665	66.6	45
57	DOW CHEMICAL	20908	84	14	14	2.9	11	3.6	20200	2052	23582	25.6	22
58	PHARMACIA & UPJOHN	20822	41	63	63	3.4	28	2.6	6949	739	11461	12.1	45
59	KIMBERLY-CLARK	20492	73	25	25	5.6	17	2.5	13789	1184	11439	33.5	45
60	SCHLUMBERGER	20260	83	28	28	4.1	30	1.8	7622	649	8910	13.6	36
61	NYNEX	20146	46	11	11	3.3	14	5.1	13407	1396	26220	22.7	55
62	MCI COMMUNICATIONS	20111	29	44	44	2.1	34	0.2	15265	548	19301	6.1	55
63	SEARS, ROEBUCK	19956	51	79	79	4.9	20	1.8	34925	1025	33130	24.9	54
64	TRAVELERS GROUP	19863	42	48	48	1.8	12	1.4	NA	1628	114475	15.3	62
65	ATLANTIC RICHFIELD	19239	120	3	3	2.9	14	4.6	15819	1376	23999	20.3	11
66	EMERSON ELECTRIC	19186	86	25	25	3.9	20	2.3	10013	929	9399	19.8	34
67	ALLSTATE	18894	42	40	40	1.5	11	2.0	17540	1811	70029	13.3	63
68	SPRINT	18459	42	53	53	3.2	15	2.4	12765	946	15196	21.3	55
69	ANHEUSER-BUSCH	18072	71	23	23	4.1	20	2.5	10341	887	10591	20.2	43
70	FIRST DATA	17841	80	38	38	5.7	37	0.1	NA	456	12218	15.3	52
71	MONSANTO	17708	152	82	82	4.7	23	2.0	8962	748	10611	20.4	22
72	COMPUTER ASSOCIATES INTERNATIONAL	17653	72	67	67	11.1	24	0.2	3505e	752e	3269	45.2c	52
73	WMX TECHNOLOGIES	17489	35	29	29	3.5	23	1.8	10248	655	18695	15.0	52
74	FIRST UNION	17266	61	25	25	1.7	12	3.4	NA	1385	96740	14.4	61
75	XEROX	16976	157	39	39	4.4	15	2.2	16611	1174	25969	29.7	33
76	LOCKHEED MARTIN	16695	84	41	41	3.1	16	1.7	22853	1018	17648	19.4	31
77	J. P. MORGAN	16261	87	23	23	1.6	12	3.7	NA	1296	184879	13.4	61
78	SARA LEE	16200	82	30	30	4.1	19	2.3	17719	804	12431	21.5	44
79	BANC ONE	16111	37	17	17	2.0	12	3.7	NA	1278	90454	16.2	61
80	CAMPBELL SOUP	16087	65	31	31	6.5	21	2.1	7278	698	6315	30.9	44
81	AIRTOUCH COMMUNICATIONS	15894	32	17	17	4.2	106	0.0	1482	132	5648	4.0	55
82	TIME WARNER	15817	40	2	2	4.3	-62	0.9	8067	-124	22132	NEG	51
83	AMGEN	15337	60	64	64	9.5	29	0.0	1940	538	2433	32.4	45
84	VIACOM	15277	42	9	9	1.4	103	0.0	11689	215	29026	1.4	51
85	US WEST COMMUNICATIONS GROUP	15534	33	32	32	4.4	13	6.1	9484	1184	16585	34.7	55
86	SOUTHERN CO.	15500	23	5	5	1.8	14	5.4	9180	1103	30554	12.9	12
87	ALLIEDSIGNAL	15382	55	36	36	4.3	17	1.0	14346	875	12465	25.1	71
88	KELLOGG	15470	73	8	8	9.9	21	2.1	7004	762	4415	48.4	44
89	WARNER-LAMBERT	15199	36	35	35	6.7	19	2.5	7040	740	6101	35.0	45
90	FEDERAL HOME LOAN MORTGAGE	14935	83	21	21	2.9	14	1.7	NA	1091	106199d	21.0r	62
91	UNION PACIFIC	14433	70	27	27	2.3	24	2.5	7486	619	19446	9.4	57
92	NIKE	14393	73	155	155	7.3	29	0.6	4761	400	3143	25.4	46
93	PACIFIC TELESIS GROUP	14299	33	25	25	6.5	12	6.5	9042	1048	15841	48.7	55
94	FIRST CHICAGO NBD	13785	44	33	33	1.7	12	3.4	NA	1150	122002	13.8	61
95	UNITED TECHNOLOGIES	13321	109	44	44	3.3	19	2.0	22802	750	15568	17.9	31
96	MEDTRONIC	13170	56	50	50	9.7	32	0.5	1742	294	1947	29.8	45

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Jeff Hudson

*Vice President of
Business Development,
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THE BUSINESS WEEK GLOBAL 1000

COUNTRY	GLOBAL RANK	MARKET VALUE \$ MIL	% CHG FROM 1995 (U.S. \$) LOCAL	BOOK VALUE RATIO	YIELD	SALES U.S. \$ MIL	PROFITS U.S. \$ MIL	ASSETS U.S. \$ MIL	RETURN ON EQUITY	STOCK CODE			
97 COMPAQ COMPUTER	223	12761	49	24	24	2.8	13	14755	1030	7818	22.0	33	
98 NORWEST	228	12761	35	23	23	2.5	12	956	72134	20.0	61		
99 RAYTHEON	229	12744	53	37	37	3.0	16	11716	793	9541	18.6	31	
100 CATERPILLAR	230	12722	66	9	9	3.8	11	16072	1136	16830	32.9	38	
101 ROCKWELL INTERNATIONAL	233	12691	28	28	34	16	2.0	12981	742	12505	21.5	35	
102 BURLINGTON NORTHERN SANTA FE	234	12679	39	39	2.5	1.4	8170	605	18269	12.7	57		
103 TELE-COMMUNICATIONS	239	12655	18	18	NA	-210	0.0	4710d	-52d	20740	NA	51	
104 H. J. HEINZ	240	12311	33	10	10	4.9	19	8087	541	8247	25.6	44	
105 BAXTER INTERNATIONAL	242	12123	40	17	17	3.2	23	5048	371	9437	10.0	45	
106 INTERNATIONAL PAPER	249	11897	40	1	1.3	26	2.5	18496d	439d	28466	NA	23	
107 MAY DEPARTMENT STORES	251	11836	47	32	32	2.6	17	10507e	700e	10122e	15.0	54	
108 GENERAL RE	252	11466	146	8	8	1.8	14	6102	825	35946	13.2	63	
109 J. C. PENNEY	254	11653	10	10	2.1	15	4.0	20562e	838e	17102e	13.9	54	
110 FLEET FINANCIAL GROUP	255	11607	44	10	1.9	26	3.9	NA	610	84432	7.4	61	
111 COLGATE-PALMOLIVE	260	11532	2	2	9.0	23	2.4	8358	541	7642	39.8	44	
112 SUN MICROSYSTEMS	261	11466	63	178	5.8	26	0.0	5902	356	3545	22.7	33	
113 AUTOMATIC DATA PROCESSING	269	11119	38	23	23	5.3	25	2894	395	3201	21.0	52	
114 MERRILL LYNCH	271	11097	38	38	2.1	10	1.9	NA	1114	176857	20.3	62	
115 McDONNELL DOUGLAS	273	11028	101	40	40	3.7	15	0.9	14332	707	10466	24.4	31
116 NORFOLK SOUTHERN	274	10988	86	26	26	2.3	15	2.6	4668	733	10905	15.0	57
117 DEERE	275	10927	44	44	3.5	14	1.9	8830	706	13847	24.9	38	
118 PHILLIPS PETROLEUM	276	10927	14	14	3.4	18	2.9	13368	518	11978	19.3	11	
119 DUN & BRADSTREET	277	10854	64	21	21	9.2	36	4.1	5415	321	5516	25.4	52
120 ALUMINUM CO. OF AMERICA	281	10821	62	33	33	2.5	14	2.2	12500	791	13643	17.5	24
121 TEXAS INSTRUMENTS	286	10659	56	-3	-3	2.6	11	1.2	13128	1088	9215	24.3	35
122 CSX	292	10470	50	30	30	2.5	14	2.1	10504	727	14231	17.7	57
123 PNC BANK	297	10376	30	13	13	1.8	12	4.6	NA	788	73404	14.7	61
124 BANK OF NEW YORK	303	10226	52	27	27	2.0	11	3.1	NA	914	53720	17.8	61
125 ARCHER DANIELS MIDLAND	304	10151	10	11	1.8	13	1.0	12672	796	9757	13.4	44	
126 DEAN WITTER, DISCOVER	305	10114	25	25	2.1	12	1.5	NA	856	38208	17.7	62	
127 ENRON	306	10083	40	10	10	3.3	19	2.1	9189	520	13239	17.8	12
128 CPC INTERNATIONAL	307	10060	69	14	14	5.6	20	2.2	8432	512	7502	28.5	44
129 ALBERTSON'S	310	10044	40	42	42	5.1	21	1.5	12585e	465e	4136e	24.5	54
130 UNITED HEALTHCARE	311	10003	47	47	3.0	25	0.1	5671	382	6161	12.2	52	
131 DUKE POWER	313	9884	16	16	2.1	15	4.2	4422	715	13358	13.7	12	
132 GANNETT	316	9884	70	30	30	4.6	22	2.0	4615	448	6504	21.1	51
133 PPG INDUSTRIES	317	9784	24	24	3.9	14	2.5	7058	743	6194	27.6	22	
134 GAP	318	9697	34	96	5.9	25	0.9	4395e	354e	2343e	23.5	54	
135 PACIFIC GAS & ELECTRIC	322	9689	-20	1.1	8.4	9622	1333	26850	13.8	12			
136 CONAGRA	325	9652	43	28	3.9	19	2.2	24109	496	10801	20.5	44	
137 WORLDCOM (7)	331	9644	49	88	4.3	34	0.0	3640	268	6635	12.7	56	
138 TENNECO	334	9351	54	12	12	3.0	12	3.3	8899	735	13451	24.2	71
139 LOEWS	336	9339	80	34	34	1.1	1.3	20133	1775	65058	23.5	71	
140 AMP	339	9239	42	-1	-1	3.3	21	2.4	5227	427	4505	15.8	35
141 TEXAS UTILITIES	340	9231	41	13	13	1.6	13	4.9	5639	663	11634	12.5	12
142 GENERAL MILLS	341	9231	57	64.5	21	3.5	5027	385	3358	302.2	44		
143 KEYCORP	343	9056	27	1.8	11	3.9	NA	89	66339	16.2	61		
144 RJR NABISCO HOLDINGS	345	9043	33	16	16	5.6	16008	627	31518	4.6	43		
145 WEYERHAEUSER	346	9005	3	3	2.1	10	3.5	11183	983	13253	20.9	23	
146 NABISCO HOLDINGS (7)	347	9005	34	30	30	2.1	28	1.6	8294	314	12303	7.6	44
147 US WEST MEDIA	349	8937	19	NA	2.0	70	0.0	2374	145	8615	2.9	55	
148 CORNING	351	8795	38	20	20	4.2	-425	1.9	5313	-10	5987	NEG	71
149 CIGNA	352	8789	115	54	54	1.2	9	1.8	13914	95903	14.3	63	
150 RHONE-POULENC RORER	353	8782	65	18	2.3	25	1.1	5142	357	8987	21.0	45	
151 CORESTATES FINANCIAL	354	8725	39	18	2.3	4.3	NA	503	29620	21.8	61		
152 CARNIVAL	355	8668	28	3.6	19	1.2	4105	19.6	53				
153 AETNA LIFE & CASUALTY	363	8495	74	24	1.2	7431	474	84324	7.5	63			
154 U. S. HEALTHCARE	368	8361	54	75	75	8.6	22	2.0	3462	1667	39.6	52	
155 FIRST BANK SYSTEM	370	8321	60	44	2.9	14	2.7	NA	568	33874	21.3	61	
156 OCCIDENTAL PETROLEUM	373	8263	26	13	13	2.5	21	3.9	10423	511	17815	12.2	71
157 SUNTRUST BANKS	374	8229	37	54	14.7	42	0.0	1295	840	34.8	33		
158 3COM	375	8204	67	35	35	4.1	19	2.3	4157	388	3613	21.1	37
159 ILLINOIS TOOL WORKS	376	8147	13	13	1.5	2.3	4147	22997	13.7	63			
160 CHUBB	377	8147	13	13	1.5	2.3	4147	22997	13.7	63			
161 UNOCAL	384	8070	33	10	10	3.3	25	2.5	7527	297	9891	13.5	11
162 ALCO STANDARD	388	8024	63	75	75	5.1	32	0.9	9892	219	4738	16.1	52
163 DIGITAL EQUIPMENT	390	8014	52	17	17	2.2	18	0.0	13813	57	9947	12.6	33
164 TOYS 'R' US	391	7931	29	14	14	2.3	19	0.0	9427e	419e	6738e	12.0	74

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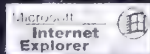
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 **TEXAS
INSTRUMENTS**

COUNTRY RANK	GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE		
165	FPL GROUP	396	7888	43	9	9	1.8	14	4.3	5592	553	12459	13.2	12
166	WALGREEN	397	7846	32	32	32	4.4	23	1.4	10395	321	3253	19.2	54
167	GOODYEAR TIRE & RUBBER	399	7830	51	20	20	2.4	12	2.0	13166	611	9790	19.3	37
168	U.S. ROBOTICS (7)	402	7803	92	340	340	13.9	55	0.0	889	66	660	25.3	55
169	AMERICAN BRANDS	404	7781	44	8	8	2.0	15	4.6	11367	523	8021	13.4	43
170	WESTINGHOUSE ELECTRIC	407	7696	18	27	27	4.8	141	1.1	6296	196	16752	3.4	34
171	BOSTON SCIENTIFIC	412	7611	43	49	49	9.9	28	0.0	1107	204	1075	35.3	45
172	MORGAN STANLEY GROUP	413	7570	50	30	30	1.8	10	1.4	NA	600i	143753	16.9	62
173	MELLON BANK	414	7566	57	34	34	2.2	13	4.2	NA	691	40646	17.4	61
174	NATIONAL CITY	416	7537	36	17	17	1.9	11	4.0	NA	465	36199	16.6	61
175	MATTEL	417	7516	27	36	36	5.9	21	0.9	3639	358	2696	27.6	46
176	AMERICAN ELECTRIC POWER	419	7489	40	17	17	1.7	13	6.0	5670	557	15902	13.0	12
177	PITNEY BOWES	425	7429	50	34	34	3.6	18	2.8	3555	408	7845	19.9	52
178	AMERICAN GENERAL	428	7370	36	3	3	1.2	11	3.7	1753	707	61153	11.9	63
179	DAYTON HUDSON	429	7346	102	44	44	2.3	23	1.7	23516e	311e	12570e	9.9	54
180	ASCEND COMMUNICATIONS (7)	430	7338	67	590	590	26.4	165	0.0	39d	9d	53d	16.0	52
181	SAFEWAY (7)	431	7324	34	85	85	8.1	22	0.0	16398	328	5194	36.3	54
182	EDISON INTERNATIONAL	432	7320	17	-5	-5	1.2	10	6.1	8383	739	23946	11.8	12
183	W. R. GRACE	433	7318	75	16	16	5.9	90	0.7	3666	65	6298	6.6	22
184	WACHOVIA	436	7245	43	13	13	1.9	12	3.4	NA	603	44981	16.0	61
185	AMR	437	7244	94	39	39	2.0	11	0.0	16910	530	19556	17.4	56
186	ITT	439	7215	62	NA	NA	2.5	50	0.0	6428	166	8692	4.9	53
187	TEXTRON	442	7175	85	39	39	2.1	15	2.1	9973	479	23172	14.3	71
188	CUC INTERNATIONAL	444	7048	37	51	51	9.6	41	0.0	1415e	163e	1141e	23.3	52
189	FEDERATED DEPARTMENT STORES	447	7001	35	51	51	1.6	25	0.0	15933e	280e	14295e	6.7	54
190	MARSH & McLENNAN	456	6838	94	18	18	4.1	16	3.4	NA	403	4330	25.3	63
191	NEWMONT GOLD	457	6834	62	54	54	7.9	80	0.8	636	90	1774	9.9	81
192	MBNA	458	6822	31	36	36	5.4	19	2.1	NA	353	13229	28.9	62
193	HOUSEHOLD INTERNATIONAL	463	6741	69	40	40	2.5	15	2.0	NA	453	29219	16.2	62
194	DOMINION RESOURCES	464	6712	38	2	2	1.4	14	6.8	4652	425	13903	9.9	12
195	APPLIED MATERIALS	465	6684	37	3	-3	3.7	10	0.0	3062	454	2965	36.0	35
196	MICRON TECHNOLOGY	466	6676	32	-28	-28	3.5	7	0.6	2953	844	2775	51.5	35
197	AIR PRODUCTS & CHEMICALS	469	6666	60	12	12	2.8	18	1.8	3865	368	5816	15.7	22
198	GEORGIA-PACIFIC	472	6599	72	-7	-7	1.9	8	2.8	14292	1018	12335	24.0	23
199	SERVICE CORP. INTERNATIONAL (7)	476	6553	56	95	95	3.3	29	0.9	1652	184	7664	11.3	52
200	CONSOLIDATED EDISON CO. OF NEW YORK	477	6550	28	-7	-7	1.2	10	7.5	6537	724	13950	12.3	12
201	PUBLIC SERVICE ENTERPRISE GROUP	482	6484	27	-11	-11	1.2	10	8.2	6164	639	17171	12.2	12
202	UNION PACIFIC RESOURCES GROUP (7)	486	6451	26	NA	NA	4.9	18	0.2	1333	351	3309	26.6	11
203	HONEYWELL	488	6428	51	28	28	3.2	19	2.0	6731	334	5060	16.8	34
204	FREEMONT-McMORAN COPPER & GOLD	489	6422	33	59	59	21.0	31	2.8	1834	281	3582	68.5	24
205	HFS (7)	492	6396	62	314	314	11.4	77	0.0	404	80	1166	14.7	53
206	HALLIBURTON	493	6386	56	49	49	3.6	26	1.8	5699	234	3647	14.1	36
207	BOATMEN'S BANCSHARES	497	6357	40	24	24	1.8	12	3.7	NA	419	33704	14.8	61
208	GENENTECH	499	6323	53	9	9	3.9	45	0.0	918	146	2011	8.6	45
209	USX-MARATHON GROUP	504	6287	22	10	10	2.2	12	3.1	13871	336	10109	18.3	11
210	RALSTON PURINA	506	6236	61	22	22	12.6	22	2.0	5622	263	4567	57.4	44
211	AVON PRODUCTS	509	6208	93	37	37	32.5	22	2.5	4492	286	2053	149.1	45
212	UST	510	6208	33	10	10	21.3	15	4.5	1300	430	785	143.2	43
213	SYSCO	511	6203	34	26	26	4.4	23	1.5	12118	252	3095	19.3	44
214	SEAGATE TECHNOLOGY	513	6192	59	64	64	2.7	10	0.0	4540	260	3361	26.5	35
215	CNA FINANCIAL	514	6180	100	17	17	0.9	7	0.0	11735	757	59902	14.1	63
216	PRAXAIR	515	6179	41	63	63	5.1	22	0.9	3146	262	4134	22.9	22
217	TRW	517	6145	94	19	19	2.8	14	2.3	10172	446	5890	20.2	37
218	BROWNING-FERRIS INDUSTRIES	522	6083	31	-14	-14	2.2	18	2.2	5779	385	7460	12.5	52
219	COX COMMUNICATIONS (7)	524	6080	23	38	38	2.6	56	0.0	1286	104	5555	4.7	51
220	HERCULES	525	6076	57	8	8	5.7	20	1.6	2427	333	2493	28.8	22
221	WM. WRIGLEY JR. (7)	526	6074	52	16	16	7.3	27	2.0	1755	224	1099	27.3	44
222	ITT HARTFORD GROUP	528	6065	52	NA	NA	1.3	11	3.1	9628	559	93855	12.2	63
223	TYCO INTERNATIONAL	532	6026	40	46	46	3.7	21	0.5	4535	248	3381	17.6	71
224	CROWN CORK & SEAL	537	5989	47	-1	-1	2.9	67	2.1	5054	75	5052	4.3	26
225	NEWMONT MINING	538	5989	60	44	44	7.6	77	0.8	792	78	1774	9.9	81
226	ENTERGY	539	5979	26	6	6	0.9	12	6.9	6274	500	22266	8.0	12
227	BANKERS TRUST NEW YORK	540	5965	75	20	20	1.4	13	5.3	NA	215	104002	10.9	61
228	ALLTEL	541	5964	32	28	28	3.1	18	3.3	3110	335	5073	17.6	55
229	MARRIOTT INTERNATIONAL	543	5961	48	40	40	5.7	24	0.7	8961	247	4018	23.1	53
230	UNICOM	546	5945	28	2	2	1.0	8	5.8	6910	660	23247	13.3	12
231	BARNETT BANKS	548	5918	63	26	26	1.9	11	3.5	NA	533	41554	16.6	61
232	PACIFICORP	549	5909	20	2	2	1.6	12	5.4	3401	505	14015	13.2	12

If you know where you're going,
you're more likely to arrive relaxed.



Let's make things better.

Bernd Wiege, Project Manager Car Systems
Wetzlar, Germany



For some people, reaching their destination quickly is all that matters. At Philips, we like to go further.

My name is Bernd Wiege, project manager for CARiN navigation systems at Philips Car Systems, Wetzlar.

CARiN is already the most successful car-navigation system in Germany where I work. Our next aim is to make it compatible with cars already on the road, and bring it to other countries.

It will mean drivers arrive quickly, economically, safely as well as by the best possible route. When we achieve that, we'll look for a new destination.



PHILIPS

THE BUSINESS WEEK GLOBAL 1000

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233	PARAMETRIC TECHNOLOGY	554	5781	46	115	15.4	57	0.0	394	77	454	27.0	52	
234	CENTRAL & SOUTH WEST	557	5781	28	7	1.7	13	6.3	5404	445	13869	13.0	12	
235	THERMO ELECTRON (7)	558	5780	64	76	76	4.1	36	0.0	2207	140	3745	11.4	35
236	CONRAIL	559	5767	70	30	30	2.0	15	2.4	3686	419	8424	13.5	57
237	UNION CARBIDE	560	5765	43	48	48	2.8	7	1.7	5888	925	6256	39.5	22
238	HOUSTON INDUSTRIES	561	5748	22	2	2	1.4	13	6.9	3680	416	11820	10.8	12
239	TELLABS (7)	562	5735	65	95	95	12.5	47	0.0	635	116	552	26.4	55
240	R. R. DONNELLEY & SONS	567	5659	17	1	1	2.6	20	2.0	6512	299	5385	13.2	52
241	TURNER BROADCASTING SYSTEM (7)	568	5656	27	37	37	28.7	114	0.3	3437	103	4395	25.3	51
242	NETSCAPE COMMUNICATIONS	570	5647	68	NA	NA	908	0.0	81	-3	228	3.3	55	
243	HERSHEY FOODS	575	5619	73	41	41	5.2	21	2.0	3691	282	2831	24.8	44
244	LIMITED	576	5619	21	-7	-7	2.7	25	1.9	7881e	349e	4570	10.8c	54
245	KMART	579	5605	12	-9	-9	1.1	-166	0.0	34389e	-100e	15397e	NEG	54
246	AMERICAN STORES	580	5602	37	43	43	2.3	17	1.7	18309e	317e	7363e	13.9	54
247	MORTON INTERNATIONAL	582	5587	38	20	20	3.4	17	1.4	3326	294	2756	20.4	22
248	DURACELL INTERNATIONAL	584	5560	47	8	8	4.3	24	2.5	2079	236	2420	18.4	46
249	GENUINE PARTS	586	5540	46	16	16	3.4	18	2.9	5262	309	2274	19.0	37
250	LOWE'S	588	5522	34	26	26	3.3	26	0.6	7075e	226e	3556e	12.9	54
251	BANK OF BOSTON	589	5512	50	37	37	1.7	11	3.5	NA	541	47397	16.3	61
252	CAROLINA POWER & LIGHT	591	5494	36	21	21	2.1	14	5.0	3007	373	8227	15.6	12
253	PECO ENERGY	592	5477	25	-12	-12	1.2	9	7.1	4186	610	14961	12.9	12
254	FIFTH THIRD BANCORP (7)	594	5473	55	54	54	3.2	18	1.9	1474	288	17053	17.6	61
255	AON	596	5461	50	38	38	2.0	19	2.9	3055	304	19736	10.8	63
256	BAY NETWORKS	599	5447	29	19	19	6.7	26	0.0	1342	131	1115	25.5	35
257	TRANSAMERICA	600	5445	81	36	36	1.4	12	2.5	NA	471	47945	11.6	62
258	FLUOR	601	5445	65	32	32	3.8	22	1.0	9301	232	3229	17.1	38
259	INTIMATE BRANDS (7)	605	5406	22	NA	NA	43.4	24	2.2	2108	203	769	184.8	54
260	DOVER	606	5406	48	45	45	4.4	18	1.3	3746	278	2667	24.1	71
261	INTERNATIONAL FLAVORS & FRAGRANCES	608	5398	49	-1	-1	4.8	22	2.8	1439	249	1534	22.0	22
262	U.S. BANCORP (7)	613	5365	36	45	45	2.2	15	3.1	2798	329	31794	14.2	61
263	BECTON, DICKINSON	614	5356	85	48	48	4.1	21	1.1	2713	252	3000	19.2	45
264	EASTMAN CHEMICAL	614	5314	67	12	12	3.5	10	2.5	5040	567	4854	34.8	22
265	DRESSER INDUSTRIES	617	5312	29	28	28	3.2	23	2.3	5613	213	4707	14.1	36
266	AMERADA HESS	619	5301	57	12	12	2.0	114	1.1	7525	-88	7756	NEG	11
267	WILLIAMS	625	5264	50	48	48	1.7	18	2.7	2856	299	10495	9.9	11
268	HILTON HOTELS	626	5260	108	61	61	4.2	30	1.1	1649	173	3060	14.1	53
269	MIRAGE RESORTS (7)	627	5248	57	92	92	4.3	30	0.0	1331	170	1792	14.3	53
270	WINN-DIXIE STORES	629	5244	35	20	20	4.2	21	2.6	11788	232	2483	20.2	54
271	CABLETRON SYSTEMS	630	5235	73	36	36	8.8	47	0.0	1070e	217e	690	19.0c	35
272	FRONTIER (7)	631	5215	32	41	41	5.4	32	2.6	2144	145	2109	16.8	55
273	NOVELL	632	5211	14	-26	-26	2.7	16	0.0	2041	338	2417	16.9	33
274	IOMEGA (7)	634	5191	44	1774	1774	70.5	279	0.0	326	9	266	25.3	33
275	AUTOZONE (7)	636	5176	35	51	51	7.2	35	0.0	1808	139	1112	20.4	54
276	DELL COMPUTER (7)	639	5150	55	120	120	5.8	19	0.0	3475d	149d	1594d	30.7	33
277	COMERICA	643	5104	44	38	38	1.9	12	3.6	NA	413	35470	16.1	61
278	EMC	646	5076	22	-4	-4	4.4	15	0.0	1921	365	1746	30.4	35
279	HBO (7)	649	5039	125	157	157	14.6	154	0.1	496	-25	535	-4.8	52
280	MASCO	653	5014	31	8	8	3.0	21	2.4	2927	248	3779	14.5	21
281	ARCO CHEMICAL	654	5005	52	12	12	2.5	10	5.4	4282	508	4135	24.8	22
282	LIBERTY MEDIA	664	4923	30	NA	NA	NA	37	0.0	1483d	128d	2232d	NA	51
283	KROGER	668	4911	39	51	51	-3.0	15	0.0	23938	319	5045	NA	54
284	LINCOLN NATIONAL	670	4900	47	4	4	1.1	10	3.9	3254	482	63258	11.1	63
285	AMERICA ONLINE (7)	677	4891	57	217	217	11.1	257	0.0	394	-34	406	4.3	52
286	PANENERGY	677	4846	32	28	28	2.2	15	3.0	4968	304	7627	14.5	12
287	NUCOR	680	4822	55	15	15	3.5	19	0.6	3462	275	2296	18.8	25
288	BURLINGTON RESOURCES	681	4807	38	-8	-8	2.2	72	1.4	873	24	4165	3.0	11
289	NEWELL	686	4762	30	21	21	3.7	22	1.9	2498	222	2931	17.0	41
290	FRANKLIN RESOURCES (7)	687	4759	59	35	35	4.0	17	0.7	867	269	2245	23.8	62
291	QUAKER OATS (7)	689	4750	35	0	0	4.4	12	3.2	6365	806	4827	35.9	44
292	CASCADE COMMUNICATIONS (7)	692	4723	56	431	431	46.3	161	0.0	135	25	112	28.7	52
293	MCGRAW-HILL	695	4715	47	27	27	4.5	20	2.8	2935	227	3104	22.2	51
294	PIONEER HI-BRED INTERNATIONAL	697	4700	57	44	44	5.2	27	1.4	1532	183	1293	19.0	26
295	CINERGY (7)	700	4671	30	12	12	1.8	13	5.8	3031	378	8220	13.8	12
296	NEXTEL COMMUNICATIONS	703	4660	21	54	54	1.7	-9	0.0	225	-331	2889d	NEG	55
297	TENET HEALTHCARE	705	4631	22	29	29	2.2	11	0.0	3318	194	7918	19.6	52
298	TIMES MIRROR	707	4612	44	88	88	3.8	59	0.9	3448	165	3817	6.4	51
299	COOPER INDUSTRIES	709	4604	43	15	15	2.7	16	3.1	4886	281	6064	16.4	71
300	INGERSOLL-RAND	711	4595	42	13	13	2.6	16	1.8	5729	270	5563	16.3	38

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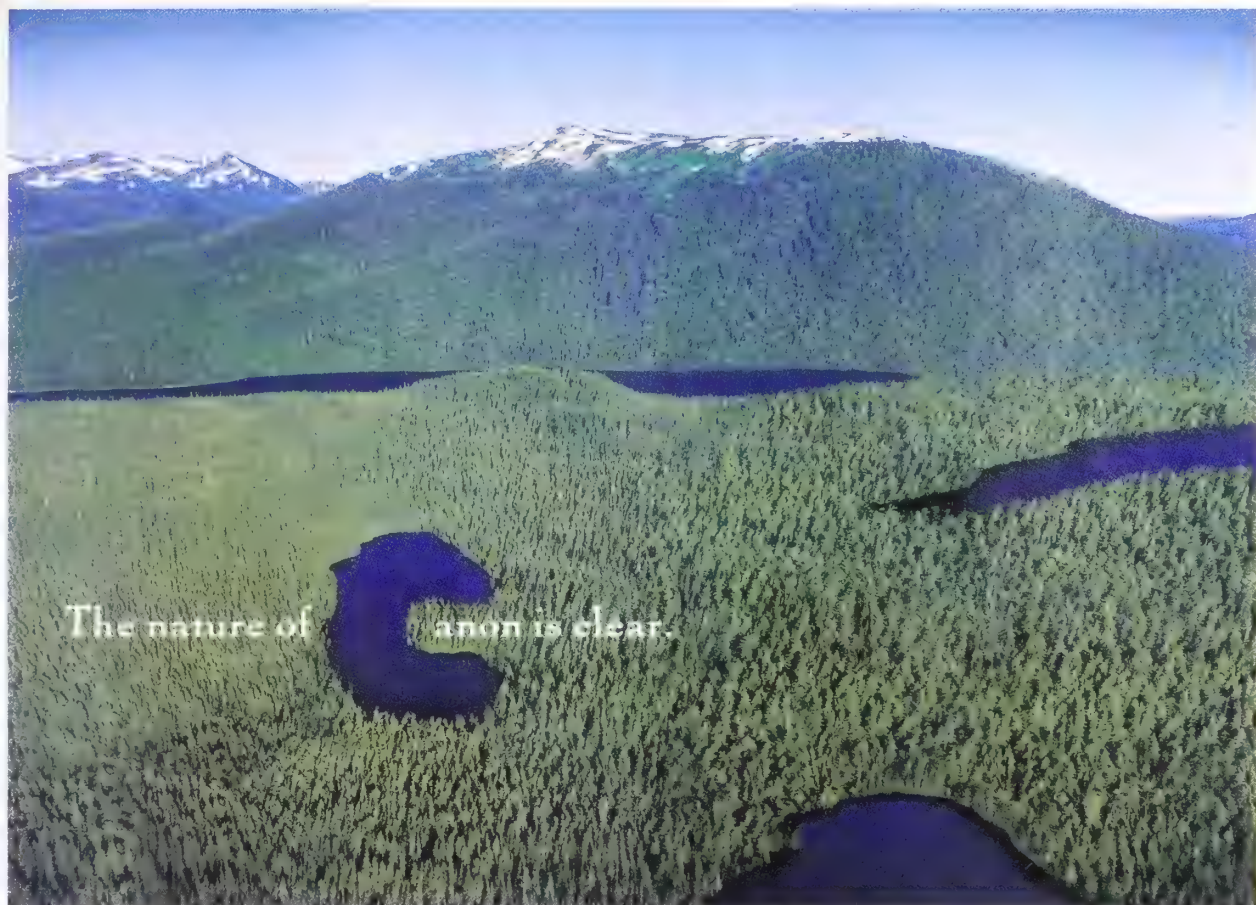
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THE BUSINESS WEEK GLOBAL 1000

COUNTRY RANK		U.S. RANK	MARKET VALUE U.S. \$ MIL	PRICE PER SHARE U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL	PROFITS U.S. \$ MIL	ASSETS U.S. \$ MIL	RETURN ON EQUITY %	INDUST CODE	
301	READER'S DIGEST ASSOCIATION	712	4570	42	2	2	7.5	20	4.2	3069	264	1959	37.5	51
302	CONSOLIDATED NATURAL GAS	714	4553	48	21	21	2.2	17	4.0	3307	212	5418	13.2	12
303	PHELPS DODGE	716	4547	69	25	25	1.8	7	2.9	4185	747	4646	26.4	24
304	DILLARD DEPARTMENT STORES	717	4531	40	39	39	1.9	26	0.3	6097e	245e	4578	7.5c	54
305	TRIBUNE	718	4520	74	24	24	4.4	22	1.6	2245	237	3288	19.9	51
306	BAKER HUGHES	721	4505	31	39	39	2.9	36	1.5	2637	120	3167	8.1	36
307	EATON	722	4503	58	-5	-5	2.3	12	2.8	6822	399	5053	19.5	37
308	ROHM & HAAS	723	4481	68	15	15	2.8	15	2.4	3884	292	3916	18.5	22
309	GREEN TREE FINANCIAL (7)	724	4476	33	50	50	4.4	17	0.8	711	254	2384	26.0	62
310	SILICON GRAPHICS	725	4470	27	-30	-30	3.4	22	0.0	2228	225	2207	15.3	33
311	EQUITABLE	726	4469	24	14	14	1.3	13	0.8	607	350	113749	10.3	63
312	ESTEE LAUDER (7)	727	4457	38	NA	NA	11.3	NA	0.2	2899	121	1722	NA	45
313	CHIRON	730	4440	105	103	103	6.5	-39	0.0	1100	512	1490	NEG	45
314	ST. PAUL	731	4430	53	4	4	1.2	9	3.3	3971	521	19657	13.2	63
315	COMPUTER SCIENCES	732	4410	79	49	49	3.8	32	0.0	4242e	142e	2334	11.9c	52
316	SALOMON	734	4405	44	2	2	1.2	8	1.5	NA	457	188428	15.3	62
317	CLOROX	736	4396	85	42	42	4.7	21	2.5	1984	201	1907	22.9	44
318	MFS COMMUNICATIONS	738	4370	35	136	136	5.2	-14	0.0	583	-267	1867	NEG	55
319	FEDERAL EXPRESS	743	4349	77	28	28	1.9	16	0.0	9392	298	6433	12.3	52
320	REPUBLIC INDUSTRIES (7)	746	4328	52	292	292	8.6	141	0.0	260	23	542	6.1	52
321	COASTAL	747	4324	41	31	31	1.6	16	1.0	10448	270	10659	10.3	11
322	UNUM	748	4323	59	38	38	1.9	14	1.9	3018	291	14788	13.1	63
323	CIRCUS CIRCUS ENTERPRISES	749	4302	42	25	25	3.5	31	0.0	1300e	129e	2212e	11.2	53
324	MELVILLE	751	4282	41	2	2	3.5	37	1.1	9689	150	3962	9.6	54
325	AFLAC	752	4282	30	8	8	2.0	13	1.3	6071	349	25338	15.8	63
326	DELTA AIR LINES	756	4261	83	27	27	2.3	9	0.2	12194	294	12143	27.0	56
327	SAFECO	760	4246	34	15	15	1.1	10	3.4	2424	399	18768	11.2	63
328	DTE ENERGY	761	4245	29	-3	-3	1.2	10	7.0	3636	438	11131	11.9	12
329	CHARLES SCHWAB	762	4243	34	39	39	6.7	24	0.7	NA	173	10552	27.8	62
330	RUBBERMAID	764	4241	28	-12	-12	3.9	30	2.0	2344	158	1692	12.8	41
331	STATE STREET BOSTON	766	4223	52	55	55	2.7	16	1.4	NA	247	25785	16.6	61
332	WHIRLPOOL	768	4220	57	0	0	2.3	25	2.4	8163	209	7800	9.2	41
333	CHAMPION INTERNATIONAL	769	4214	44	-5	-5	1.2	6	0.5	6972	751	9543	19.2	23
334	SALLIE MAE	770	4202	74	57	57	4.9	13	2.2	NA	371	50002	39.3	62
335	GUIDANT (7)	773	4176	58	146	146	12.1	38	0.2	862d	92d	1104d	31.6	45
336	GREAT LAKES CHEMICAL	775	4162	65	6	6	2.9	14	0.7	2361	296	2469	20.6	22
337	NORDSTROM	778	4146	51	23	23	2.9	25	1.0	4114e	165e	2733e	11.5	54
338	COMCAST	780	4110	17	0	0	-5.0	58	0.5	3363	-38	9580	NA	51
339	PROVIDIAN	787	4077	44	20	20	1.4	11	2.3	1195	345	26839	12.7	63
340	BALTIMORE GAS & ELECTRIC	791	4039	27	5	5	1.4	12	5.8	2935	338	8317	11.6	12
341	STRATACOM (7)	792	4038	54	184	184	15.3	76	0.0	332	52	295	20.1	55
342	ENRON OIL & GAS (7)	793	4036	25	4	4	3.5	29	0.5	586	142	2147	12.0	11
343	GENERAL PUBLIC UTILITIES	794	4036	34	12	12	1.4	10	5.8	3805	344	9870	13.0	12
344	UNION ELECTRIC	796	4031	39	4	4	1.7	13	6.3	2103	314	6754	13.0	12
345	LSI LOGIC (7)	798	4009	31	-8	-8	3.3	17	0.0	1268	238	1850	18.9	35
346	OFFICE DEPOT	800	3995	26	6	6	4.0	30	0.0	5313	132	2531	13.2	54
347	SOUTHWEST AIRLINES	808	3961	27	24	24	2.9	20	0.2	2873	183	3256	13.8	56
348	COCA-COLA ENTERPRISES	816	3916	49	49	49	2.9	53	0.3	6773	77	9064	5.5	43
349	PRICE/COSTCO	818	3906	20	42	42	2.6	18	0.0	18247	217	4437	14.4	54
350	GENERAL INSTRUMENT	820	3894	31	0	0	4.2	20	0.0	2432	214	2301	20.8	35
351	GENERAL DYNAMICS	821	3892	62	41	41	2.5	15	2.7	3067	247	3164	16.1	31
352	VF	823	3884	61	14	14	2.2	15	2.4	5062	260	3447	14.3	47
353	SHERWIN-WILLIAMS	833	3843	45	22	22	3.2	19	1.6	3274	201	2141	16.6	22
354	NORTHWEST AIRLINES (7)	835	3842	40	40	40	-5.5	11	0.0	9085	342	8412	-55.9	56
355	DOW JONES	838	3817	39	7	7	2.4	21	2.5	2284	190	2599	11.4	51
356	SOUTHERN PACIFIC RAIL	840	3806	34	54	54	3.0	152	0.0	3151	36	4749	2.4	57
357	PP&L RESOURCES	857	3677	23	19	19	1.4	11	7.3	2752	323	9492	13.1	12
358	INTERPUBLIC GROUP	858	3674	46	26	26	4.9	21	1.5	2180	168	4260	23.2	52
359	JEFFERSON-PILOT	860	3660	51	46	46	1.7	13	2.8	810	254	16478	12.6	63
360	KNIGHT-RIDDER	861	3656	75	35	35	3.3	25	2.0	2855	182	3006	13.2	51
361	SONAT	864	3651	47	29	29	2.5	30	2.5	1990	114	3511	8.2	12
362	EQUIFAX (7)	866	3644	58	58	58	10.3	24	1.3	1623	148	1054	43.1	62
363	UNION CAMP	868	3639	53	1	1	1.7	9	3.4	4212	451	4838	18.9	23
364	CASE (7)	870	3629	50	54	54	2.2	11	0.4	4937	346	5469	21.4	38
365	HARLEY DAVIDSON	872	3623	48	97	97	7.3	30	0.4	1350	111	1001	24.4	46
366	THERMO INSTRUMENT SYSTEMS (7)	874	3619	39	106	106	6.1	37	0.0	783	79	1373	16.7	34
367	CERIDIAN	875	3616	53	64	64	24.5	38	0.0	1333	98	1126	63.9	52
368	H&R BLOCK	877	3606	35	-3	-3	5.3	39	3.7	1360	107	1078	13.6	52



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COUNTRY		MARKET CAP. U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE		
369	HARCOURT GENERAL	878	3606	51	20	20	3.9	22	1.3	3035	178	2884	18.2	71
370	FIRSTAR (7)	880	3588	49	55	55	2.4	16	3.1	1718	229	19168	14.7	61
371	BLACK & DECKER	884	3578	41	25	25	2.8	24	1.2	4766	217	5545	11.8	46
372	HUMANA	885	3573	22	4	4	2.8	18	0.0	5968	200	2878	15.5	52
373	FORE SYSTEMS (7)	888	3563	41	209	209	10.6	352	0.0	76	7	79	3.0	52
374	E. W. SCRIPPS (7)	889	3563	45	44	44	3.0	38	1.2	1030	94	1656	7.9	51
375	FOOD LION (7)	890	3561	8	18	18	3.3	20	1.5	8211	172	2645	16.1	54
376	TYSON FOODS (7)	891	3551	25	10	10	2.3	20	0.5	5511	219	4444	11.5	44
377	ALLEGHENY POWER SYSTEM	892	3546	29	18	18	1.7	14	5.7	2648	240	6447	12.0	12
378	CINCINNATI BELL (7)	893	3543	53	114	114	7.4	47	1.5	1336	-25	1592	15.9	55
379	OXFORD HEALTH PLANS (7)	894	3539	47	87	87	13.3	57	0.0	1766	52	609	23.2	52
380	VASTAR RESOURCES (7)	895	3537	36	15	15	34.5	27	0.8	1993	103	1552	130.1	11
381	REPUBLIC NEW YORK	896	3525	63	23	23	1.5	13	2.4	NA	289	43882	11.1	61
382	QUALCOMM	897	3522	54	112	112	4.4	113	0.0	387	30	941	3.9	34
383	ENGELHARD	899	3521	25	-12	-12	4.8	25	1.5	2840	138	1646	19.5	22
384	DSC COMMUNICATIONS	900	3495	30	-19	-19	3.1	22	0.0	1422	193	1865	14.1	34
385	PEOPLESOFT (7)	904	3477	71	186	186	20.2	115	0.0	113d	15d	172d	17.5	52
386	HARRAH'S ENTERTAINMENT	907	3457	34	14	14	5.9	43	0.0	1550	79	1637	13.7	53
387	FIRST USA (7)	908	3455	58	23	23	4.1	17	0.4	1082	175	6292	24.6	62
388	ATMEL (7)	909	3451	36	61	61	5.8	25	0.0	634	114	920	23.0	35
389	MGIC INVESTMENT (7)	911	3444	59	25	25	3.4	16	0.3	510d	160d	1476d	21.4	62
390	REYNOLDS METALS	912	3438	54	9	9	1.6	11	2.6	7213	389	7740	14.2	26
391	WASHINGTON POST	913	3434	313	18	18	2.9	18	1.5	1719	190	1733	16.1	51
392	W. W. GRAINGER	919	3409	67	12	12	2.9	18	1.5	3277	187	1669	16.0	34
393	DANA	920	3405	34	19	19	2.9	11	3.0	7598	288	5694	26.4	37
394	SUNAMERICA	931	3342	56	64	64	3.4	16	1.1	NA	194	16844	20.8	62
395	PROGRESSIVE (7)	934	3339	46	22	22	2.3	14	0.5	3004	251	5353	16.6	63
396	INFORMIX (7)	935	3338	23	8	8	6.8	32	0.0	709	105	674	21.5	52
397	RAYCHEM	936	3337	75	105	105	4.4	36	0.5	1531	34	1455	12.1	35
398	HEALTHSOUTH (7)	937	3336	35	103	103	6.1	51	0.0	1127d	53d	1552d	11.8	52
399	UAL	938	3329	57	99	99	-12.0	10	0.0	14943	391	11641	NA	56
400	CINCINNATI FINANCIAL (7)	943	3315	60	13	13	1.2	15	2.3	1656	227	5109	8.2	62
401	WILLAMETTE INDUSTRIES (7)	944	3314	60	19	19	1.7	7	2.1	3874	515	3414	25.7	23
402	HUNTINGTON BANCSHARES (7)	945	3293	25	32	32	2.2	13	3.2	1649	244	20255	16.3	61
403	HASBRO	952	3286	38	7	7	2.2	21	1.1	2858	156	2616	10.2	46
404	TANDY	954	3273	54	16	16	2.2	18	1.5	5839	212	2722	12.5	54
405	WESTERN ATLAS	955	3264	61	36	36	2.4	32	0.0	2226	100	2489	7.5	36
406	TOTAL SYSTEM SERVICES (7)	956	3264	25	254	254	22.6	112	0.2	250	28	199	20.1	52
407	MBIA	957	3263	76	21	21	1.4	11	1.8	215	271	7267	12.5	63
408	EXEL	962	3262	69	48	48	1.6	10	2.9	558	333	4721	16.1	63
409	ANDREW (7)	965	3261	54	67	67	8.3	42	0.0	626	68	491	19.8	35
410	OMNICOM GROUP (7)	967	3257	44	51	51	5.9	22	1.6	2258	140	3528	26.4	52
411	WESTVACO	968	3251	32	12	12	1.6	11	2.8	3272	283	4253	14.3	23
412	IVAX (7)	969	3246	28	7	7	3.9	26	0.4	1260	115	1335	15.0	45
413	APPLE COMPUTER	970	3232	28	-37	-37	1.1	19	1.8	11062	424	6231	NEG	33
414	NORTHERN STATES POWER	971	3229	47	1	1	1.6	12	5.7	2569	276	6229	13.0	12
415	ITT INDUSTRIES	972	3226	27	NA	NA	5.1	1369	2.2	8884	21	5879	0.4	37
416	NEW YORK TIMES	987	3213	33	46	45	1.9	23	1.7	2409	136	3377	8.8	51
417	GOLDEN WEST FINANCIAL	989	3207	55	12	12	1.4	12	0.7	NA	235	35118	11.4	61
418	MOLEX (7)	990	3205	32	7	7	2.9	22	0.2	1198	124	1441	13.0	35
419	FLORIDA PROGRESS (7)	994	3194	33	4	4	1.5	13	6.2	3056	249	5791	11.6	12
420	GARTNER GROUP (7)	995	3185	36	199	199	32.2	97	0.0	229	26	301	33.4	52
421	ANALOG DEVICES	996	3184	38	18	18	4.8	22	0.0	942	119	1002	21.6	35
422	CIRCUIT CITY STORES	999	3183	33	19	19	3.6	18	0.4	7029e	179e	2004	20.0c	54

KEY TO INDUSTRY CODES Left-hand digit represents broad economic sector as defined by Morgan Stanley Capital International. Right-hand digit is industry classification code within each economic sector

- | | | | |
|---|--|--|--|
| <p>1. ENERGY</p> <p>11. Energy sources</p> <p>12. Utilities-electrical & gas</p> <p>2. MATERIALS</p> <p>21. Building materials & components</p> <p>22. Chemicals</p> <p>23. Forest products & paper</p> <p>24. Metals-nonferrous</p> <p>25. Metals-steel</p> <p>26. Misc. materials & commodities</p> <p>3. CAPITAL EQUIPMENT</p> <p>31. Aerospace & military technology</p> | <p>32. Construction & housing</p> <p>33. Data processing & reproduction</p> <p>34. Electrical & electronics</p> <p>35. Electronic components & instruments</p> <p>36. Energy equipment & services</p> <p>37. Industrial components</p> <p>38. Machinery & engineering</p> <p>4. CONSUMER GOODS</p> <p>41. Appliances & household durables</p> <p>42. Automobiles</p> <p>43. Beverages & tobacco</p> | <p>44. Food & household products</p> <p>45. Health & personal care</p> <p>46. Recreation, other consumer goods</p> <p>47. Textiles & apparel</p> <p>5. SERVICES</p> <p>51. Broadcasting & publishing</p> <p>52. Business & public services</p> <p>53. Leisure & tourism</p> <p>54. Merchandising</p> <p>55. Telecommunications</p> <p>56. Transportation-airlines</p> | <p>57. Transportation-road & rail</p> <p>58. Transportation-shipping</p> <p>59. Wholesale & international trade</p> <p>6. FINANCE</p> <p>61. Banking</p> <p>62. Financial services</p> <p>63. Insurance</p> <p>64. Real estate</p> <p>7. OTHER</p> <p>71. Multi-industry</p> <p>81. Gold mines</p> |
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343 Kimberly-Clark (US-59)	355 Murata Mfg (JA-85)	451 Pioneer Electronic (JA-183)	460 Shin-Etsu Chemical (JA-114)	611 TOTAL (FR-5)
344 Kmart (US-245)	347 Nabisco Holdings (US-146)	452 Pioneer Hi-Bred International (US-294)	600 Sinochem (CN-1)	600 Total System Services (US-406)
345 Knight-Ridder (US-360)	348 Nagoya Railroad (JA-176)	453 Pioneer Bowles (US-177)	295 Shizuoka Bank (JA-68)	658 Toto (JA-149)
346 Kobe Steel (JA-97)	349 National Australia Bank (AS-3)	454 Placer Dome (CA-9)	932 Showa Shell Sekyuu (JA-184)	400 Toyo Seikan Kaisha (JA-108)
347 Kinn Brewery (JA-53)	350 National City (US-174)	297 PNC Bank (US-123)	512 Siemens (GE-2)	402 Toyo Trust & Banking (JA-105)
348 Kinn Brewery (JA-53)	351 National Gnu Group (BR-69)	298 Polygram (NE-9)	600 Siemens (GE-2)	563 Toyota Automatic Loom Works (JA-133)
349 Kmart (US-245)	352 National Power (BR-36)	299 Procter & Gamble (US-10)	219 Singapore Airlines (SI-2)	8 Toyota Motor (JA-3)
350 Knight-Ridder (US-360)	353 National Westminster Bank (BR-14)	300 Progressive (US-395)	498 Singapore Press Holdings (SI-6)	393 Toys 'R' Us (US-164)
351 Kobe Steel (JA-97)	354 NationsBank (US-48)	301 Promise (US-150)	34 Singapore Telecommunications (SI-1)	521 Tracelabel (BE-3)
352 NEC (JA-39)	355 NEC (JA-39)	675 Procter & Gamble (US-10)	37 Skandinaviska Enskilda Banken (SWE-10)	600 Transamerica (US-257)
353 Netscape Communications (US-242)	356 Next (BR-91)	767 Procter & Gamble (US-10)	783 SMC (JA-156)	130 Tribune (US-305)
354 Land Securities (BR-64)	357 Nextel Communications (US-296)	302 Procter & Gamble (US-10)	91 Smith & Nephew (BR-88)	517 TRW (US-217)
355 Land Securities (BR-64)	358 NGK Insulators (JA-186)	303 Procter & Gamble (US-10)	72 SmithKline Beecham (BR-6)	568 Turner Broadcasting System (US-241)
356 Land Securities (BR-64)	359 Nippon Credit Bank (JA-121)	304 Procter & Gamble (US-10)	55 Smiths Industries (BR-90)	532 Tyco International (US-223)
357 Land Securities (BR-64)	360 Nippon Express (JA-63)	305 Procter & Gamble (US-10)	331 Societe Generale (FR-12)	891 Tyson Foods (US-376)
358 Land Securities (BR-64)	361 Nippon Fire & Marine (JA-193)	306 Procter & Gamble (US-10)	65 Societe Generale de Belgique (BE-5)	
359 Land Securities (BR-64)	362 Nippon Meat Packers (JA-216)	307 Procter & Gamble (US-10)	656 Solvay (BE-7)	
360 Land Securities (BR-64)	363 Nippon Paper Industries (JA-125)	308 Procter & Gamble (US-10)	664 Sony (JA-18)	
361 Land Securities (BR-64)	364 Nippon Steel (JA-21)	309 Procter & Gamble (US-10)	598 Sony Music Entertainment (JA-140)	
362 Land Securities (BR-64)	365 Nippon Telegraph & Telephone (JA-1)	310 Procter & Gamble (US-10)	1000 Southern Co. (US-86)	
363 Land Securities (BR-64)	366 Nippon Television Network (JA-204)	311 Procter & Gamble (US-10)	840 Southern Pacific Rail (US-356)	
364 Land Securities (BR-64)	367 Nippon Yusen Kaisha (JA-93)	312 Procter & Gamble (US-10)	808 Southwest Airlines (US-347)	
365 Land Securities (BR-64)	368 Nippon Yusen Kaisha (JA-93)	313 Procter & Gamble (US-10)	558 Soarbank Sverige (SWE-19)	
366 Land Securities (BR-64)	369 Nippon Yusen Kaisha (JA-93)	314 Procter & Gamble (US-10)	143 Sprint (US-68)	
367 Land Securities (BR-64)	370 Nippon Yusen Kaisha (JA-93)	315 Procter & Gamble (US-10)	731 St. Paul (US-314)	
368 Land Securities (BR-64)	371 Nippon Yusen Kaisha (JA-93)	316 Procter & Gamble (US-10)	232 Standard Chartered (BR-34)	
369 Land Securities (BR-64)	372 Nippon Yusen Kaisha (JA-93)	317 Procter & Gamble (US-10)	766 State Street Boston (US-331)	
370 Land Securities (BR-64)	373 Nippon Yusen Kaisha (JA-93)	318 Procter & Gamble (US-10)	150 STET (IT-3)	
371 Land Securities (BR-64)	374 Nippon Yusen Kaisha (JA-93)	319 Procter & Gamble (US-10)	754 Stora Kopparbergs Bergslags (SWE-9)	
372 Land Securities (BR-64)	375 Nippon Yusen Kaisha (JA-93)	320 Procter & Gamble (US-10)	792 StrataCom (US-341)	
373 Land Securities (BR-64)	376 Nippon Yusen Kaisha (JA-93)	321 Procter & Gamble (US-10)	518 Suez (Compagnie de) (FR-21)	
374 Land Securities (BR-64)	377 Nippon Yusen Kaisha (JA-93)	322 Procter & Gamble (US-10)	16 Sumitomo Chemical (JA-94)	
375 Land Securities (BR-64)	378 Nippon Yusen Kaisha (JA-93)	323 Procter & Gamble (US-10)	383 Sumitomo Chemical (JA-94)	
376 Land Securities (BR-64)	379 Nippon Yusen Kaisha (JA-93)	324 Procter & Gamble (US-10)	251 Sumitomo Electric Industries (JA-77)	
377 Land Securities (BR-64)	380 Nippon Yusen Kaisha (JA-93)	325 Procter & Gamble (US-10)	533 Sumitomo Marine & Fire (JA-129)	
378 Land Securities (BR-64)	381 Nippon Yusen Kaisha (JA-93)	326 Procter & Gamble (US-10)	321 Sumitomo Metal Industries (JA-76)	
379 Land Securities (BR-64)	382 Nippon Yusen Kaisha (JA-93)	327 Procter & Gamble (US-10)	620 Sumitomo Metal Mining (JA-142)	
380 Land Securities (BR-64)	383 Nippon Yusen Kaisha (JA-93)	328 Procter & Gamble (US-10)	598 Sumitomo Realty & Development (JA-225)	
381 Land Securities (BR-64)	384 Nippon Yusen Kaisha (JA-93)	329 Procter & Gamble (US-10)	158 Sumitomo Trust & Banking (JA-37)	
382 Land Securities (BR-64)	385 Nippon Yusen Kaisha (JA-93)	330 Procter & Gamble (US-10)	621 Svenska Cellulosa Aktiebolaget (SWE-14)	
383 Land Securities (BR-64)	386 Nippon Yusen Kaisha (JA-93)	331 Procter & Gamble (US-10)	701 Svenska Cellulosa Aktiebolaget (SWE-14)	
384 Land Securities (BR-64)	387 Nippon Yusen Kaisha (JA-93)	332 Procter & Gamble (US-10)	207 Swire Pacific (HK-6)	
385 Land Securities (BR-64)	388 Nippon Yusen Kaisha (JA-93)	333 Procter & Gamble (US-10)	217 Swiss Bank Corp. (SWI-8)	
386 Land Securities (BR-64)	389 Nippon Yusen Kaisha (JA-93)	334 Procter & Gamble (US-10)	216 Swiss Re (SWI-7)	
387 Land Securities (BR-64)	390 Nippon Yusen Kaisha (JA-93)	335 Procter & Gamble (US-10)	814 Swiss Re (SWI-7)	
388 Land Securities (BR-64)	391 Nippon Yusen Kaisha (JA-93)	336 Procter & Gamble (US-10)	772 Synthelabo (FR-34)	
389 Land Securities (BR-64)	392 Nippon Yusen Kaisha (JA-93)	337 Procter & Gamble (US-10)	511 Sysco (US-213)	
390 Land Securities (BR-64)	393 Nippon Yusen Kaisha (JA-93)	338 Procter & Gamble (US-10)		
391 Land Securities (BR-64)	394 Nippon Yusen Kaisha (JA-93)	339 Procter & Gamble (US-10)		
392 Land Securities (BR-64)	395 Nippon Yusen Kaisha (JA-93)	340 Procter & Gamble (US-10)		
393 Land Securities (BR-64)	396 Nippon Yusen Kaisha (JA-93)	341 Procter & Gamble (US-10)		
394 Land Securities (BR-64)	397 Nippon Yusen Kaisha (JA-93)	342 Procter & Gamble (US-10)		
395 Land Securities (BR-64)	398 Nippon Yusen Kaisha (JA-93)	343 Procter & Gamble (US-10)		
396 Land Securities (BR-64)	399 Nippon Yusen Kaisha (JA-93)	344 Procter & Gamble (US-10)		
397 Land Securities (BR-64)	400 Nippon Yusen Kaisha (JA-93)	345 Procter & Gamble (US-10)		
398 Land Securities (BR-64)	401 Nippon Yusen Kaisha (JA-93)	346 Procter & Gamble (US-10)		
399 Land Securities (BR-64)	402 Nippon Yusen Kaisha (JA-93)	347 Procter & Gamble (US-10)		
400 Land Securities (BR-64)	403 Nippon Yusen Kaisha (JA-93)	348 Procter & Gamble (US-10)		
401 Land Securities (BR-64)	404 Nippon Yusen Kaisha (JA-93)	349 Procter & Gamble (US-10)		
402 Land Securities (BR-64)	405 Nippon Yusen Kaisha (JA-93)	350 Procter & Gamble (US-10)		
403 Land Securities (BR-64)	406 Nippon Yusen Kaisha (JA-93)	351 Procter & Gamble (US-10)		
404 Land Securities (BR-64)	407 Nippon Yusen Kaisha (JA-93)	352 Procter & Gamble (US-10)		
405 Land Securities (BR-64)	408 Nippon Yusen Kaisha (JA-93)	353 Procter & Gamble (US-10)		
406 Land Securities (BR-64)	409 Nippon Yusen Kaisha (JA-93)	354 Procter & Gamble (US-10)		
407 Land Securities (BR-64)	410 Nippon Yusen Kaisha (JA-93)	355 Procter & Gamble (US-10)		
408 Land Securities (BR-64)	411 Nippon Yusen Kaisha (JA-93)	356 Procter & Gamble (US-10)		
409 Land Securities (BR-64)	412 Nippon Yusen Kaisha (JA-93)	357 Procter & Gamble (US-10)		
410 Land Securities (BR-64)	413 Nippon Yusen Kaisha (JA-93)	358 Procter & Gamble (US-10)		
411 Land Securities (BR-64)	414 Nippon Yusen Kaisha (JA-93)	359 Procter & Gamble (US-10)		
412 Land Securities (BR-64)	415 Nippon Yusen Kaisha (JA-93)	360 Procter & Gamble (US-10)		
413 Land Securities (BR-64)	416 Nippon Yusen Kaisha (JA-93)	361 Procter & Gamble (US-10)		
414 Land Securities (BR-64)	417 Nippon Yusen Kaisha (JA-93)	362 Procter & Gamble (US-10)		
415 Land Securities (BR-64)	418 Nippon Yusen Kaisha (JA-93)	363 Procter & Gamble (US-10)		
416 Land Securities (BR-64)	419 Nippon Yusen Kaisha (JA-93)	364 Procter & Gamble (US-10)		
417 Land Securities (BR-64)	420 Nippon Yusen Kaisha (JA-93)	365 Procter & Gamble (US-10)		
418 Land Securities (BR-64)	421 Nippon Yusen Kaisha (JA-93)	366 Procter & Gamble (US-10)		
419 Land Securities (BR-64)	422 Nippon Yusen Kaisha (JA-93)	367 Procter & Gamble (US-10)		
420 Land Securities (BR-64)	423 Nippon Yusen Kaisha (JA-93)	368 Procter & Gamble (US-10)		
421 Land Securities (BR-64)	424 Nippon Yusen Kaisha (JA-93)	369 Procter & Gamble (US-10)		
422 Land Securities (BR-64)	425 Nippon Yusen Kaisha (JA-93)	370 Procter & Gamble (US-10)		
423 Land Securities (BR-64)	426 Nippon Yusen Kaisha (JA-93)	371 Procter & Gamble (US-10)		
424 Land Securities (BR-64)	427 Nippon Yusen Kaisha (JA-93)	372 Procter & Gamble (US-10)		
425 Land Securities (BR-64)	428 Nippon Yusen Kaisha (JA-93)	373 Procter & Gamble (US-10)		
426 Land Securities (BR-64)	429 Nippon Yusen Kaisha (JA-93)	374 Procter & Gamble (US-10)		
427 Land Securities (BR-64)	430 Nippon Yusen Kaisha (JA-93)	375 Procter & Gamble (US-10)		
428 Land Securities (BR-64)	431 Nippon Yusen Kaisha (JA-93)	376 Procter & Gamble (US-10)		
429 Land Securities (BR-64)	432 Nippon Yusen Kaisha (JA-93)	377 Procter & Gamble (US-10)		
430 Land Securities (BR-64)	433 Nippon Yusen Kaisha (JA-93)	378 Procter & Gamble (US-10)		
431 Land Securities (BR-64)	434 Nippon Yusen Kaisha (JA-93)	379 Procter & Gamble (US-10)		
432 Land Securities (BR-64)	435 Nippon Yusen Kaisha (JA-93)	380 Procter & Gamble (US-10)		
433 Land Securities (BR-64)	436 Nippon Yusen Kaisha (JA-93)	381 Procter & Gamble (US-10)		
434 Land Securities (BR-64)	437 Nippon Yusen Kaisha (JA-93)	382 Procter & Gamble (US-10)		
435 Land Securities (BR-64)	438 Nippon Yusen Kaisha (JA-93)	383 Procter & Gamble (US-10)		
436 Land Securities (BR-64)	439 Nippon Yusen Kaisha (JA-93)	384 Procter & Gamble (US-10)		
437 Land Securities (BR-64)	440 Nippon Yusen Kaisha (JA-93)	385 Procter & Gamble (US-10)		
438 Land Securities (BR-64)	441 Nippon Yusen Kaisha (JA-93)	386 Procter & Gamble (US-10)		
439 Land Securities (BR-64)	442 Nippon Yusen Kaisha (JA-93)	387 Procter & Gamble (US-10)		
440 Land Securities (BR-64)	443 Nippon Yusen Kaisha (JA-93)	388 Procter & Gamble (US-10)		
441 Land Securities (BR-64)	444 Nippon Yusen Kaisha (JA-93)	389 Procter & Gamble (US-10)		
442 Land Securities (BR-64)	445 Nippon Yusen Kaisha (JA-93)	390 Procter & Gamble (US-10)		
443 Land Securities (BR-64)	446 Nippon Yusen Kaisha (JA-93)	391 Procter & Gamble (US-10)		
444 Land Securities (BR-64)	447 Nippon Yusen Kaisha (JA-93)	392 Procter & Gamble (US-10)		
445 Land Securities (BR-64)	448 Nippon Yusen Kaisha (JA-93)	393 Procter & Gamble (US-10)		
446 Land Securities (BR-64)	449 Nippon Yusen Kaisha (JA-93)	394 Procter & Gamble (US-10)		
447 Land Securities (BR-64)	450 Nippon Yusen Kaisha (JA-93)	395 Procter & Gamble (US-10)		
448 Land Securities (BR-64)	451 Nippon Yusen Kaisha (JA-93)	396 Procter & Gamble (US-10)		
449 Land Securities (BR-64)	452 Nippon Yusen Kaisha (JA-93)	397 Procter & Gamble (US-10)		
450 Land Securities (BR-64)	453 Nippon Yusen Kaisha (JA-93)	398 Procter & Gamble (US-10)		
451 Land Securities (BR-64)	454 Nippon Yusen Kaisha (JA-93)	399 Procter & Gamble (US-10)		
452 Land Securities (BR-64)	455 Nippon Yusen Kaisha (JA-93)	400 Procter & Gamble (US-10)		
453 Land Securities (BR-64)	456 Nippon Yusen Kaisha (JA-93)	401 Procter & Gamble (US-10)		
454 Land Securities (BR-64)	457 Nippon Yusen Kaisha (JA-93)	402 Procter & Gamble (US-10)		
455 Land Securities (BR-64)	458 Nippon Yusen Kaisha (JA-93)	403 Procter & Gamble (US-10)		
456 Land Securities (BR-64)	459 Nippon Yusen Kaisha (JA-93)	404 Procter & Gamble (US-10)		
457 Land Securities (BR-64)	460 Nippon Yusen Kaisha (JA-93)	405 Procter & Gamble (US-10)		
458 Land Securities (BR-64)	461 Nippon Yusen Kaisha (JA-93)	406 Procter & Gamble (US-10)		
459 Land Securities (BR-64)	462 Nippon Yusen Kaisha (JA-93)	407 Procter & Gamble (US-10)		
460 Land Securities (BR-64)	463 Nippon Yusen Kaisha (JA-93)	408 Procter & Gamble (US-10)		
461 Land Securities (BR-64)	464 Nippon Yusen Kaisha (JA-93)	409 Procter & Gamble (US-10)		
462 Land Securities (BR-64)	465 Nippon Yusen Kaisha (JA-93)	410 Procter & Gamble (US-10)		
463 Land Securities (BR-64)	466 Nippon Yusen Kaisha (JA-93)	411 Procter & Gamble (US-10)		
464 Land Securities (BR-64)	467 Nippon Yusen Kaisha (JA-93)	412 Procter & Gamble (US-10)		
465 Land Securities (BR-64)	468 Nippon Yusen Kaisha (JA-93)	413 Procter & Gamble (US-10)		
466 Land Securities (BR-64)	469 Nippon Yusen Kaisha (JA-93)	414 Procter & Gamble (US-10)		
467 Land Securities (BR-64)	470 Nippon Yusen Kaisha (JA-93)	415 Procter & Gamble (US-10)		
468 Land Securities (BR-64)	471 Nippon Yusen Kaisha (JA-93)	416 Procter & Gamble (US-10)		
469 Land Securities (BR-64)	472 Nippon Yusen Kaisha (JA-93)	417 Procter & Gamble (US-10)		
470 Land Securities (BR-64)	473 Nippon Yusen Kaisha (JA-93)	418 Procter & Gamble (US-10)		
471 Land Securities (BR-64)	474 Nippon Yusen Kaisha (JA-93)	419 Procter & Gamble (US-10)		
472 Land Securities (BR-64)	475 Nippon Yusen Kaisha (JA-93)	420 Procter & Gamble (US-10)		
473 Land Securities (BR-64)	476 Nippon Yusen Kaisha (JA-93)	421 Procter & Gamble (US-10)		
474 Land Securities (BR-64)	477 Nippon Yusen Kaisha (JA-93)	422 Procter & Gamble (US-10)		
475 Land Securities (BR-64)	478 Nippon Yusen Kaisha (JA-93)	423 Procter & Gamble (US-10)		
476 Land Securities (BR-64)	479 Nippon Yusen Kaisha (JA-93)	424 Procter & Gamble (US-10)		
477 Land Securities (BR-64)	480 Nippon Yusen Kaisha (JA-93)	425 Procter & Gamble (US-10)		
478 Land Securities (BR-64)	481 Nippon Yusen Kaisha (JA-93)	426 Procter & Gamble (US-10)		
479 Land Securities (BR-64)	482 Nippon Yusen Kaisha (JA-93)	427 Procter & Gamble (US-10)		
480 Land Securities (BR-64)	483 Nippon Yusen Kaisha (JA-93)	428 Procter & Gamble (US-10)		
481 Land Securities (BR-64)	484 Nippon Yusen Kaisha (JA-93)	429 Procter & Gamble (US-10)		
482 Land Securities (BR-64)	485 Nippon Yusen Kaisha (JA-93)	430 Procter & Gamble (US-10)		
483 Land Securities (BR-64)	486 Nippon Yusen Kaisha (JA-93)	431 Procter & Gamble (US-10)		
484 Land Securities (BR-64)	487 Nippon Yusen Kaisha (JA-93)	432 Procter & Gamble (US-10)		
485 Land Securities (BR-64)	488 Nippon Yusen Kaisha (JA-93)	433 Procter & Gamble (US-10)		
486 Land Securities (BR-64)	489 Nippon Yusen Kaisha (JA-93)	434 Procter & Gamble (US-10)		
487 Land Securities (BR-64)	490 Nippon Yusen Kaisha (JA-93)	435 Procter & Gamble (US-10)		
488 Land Securities (BR-64)	491 Nippon Yusen Kaisha (JA-93)	436 Procter & Gamble (US-10)		
489 Land Securities (BR-64)	492 Nippon Yusen Kaisha (JA-93)	437 Procter & Gamble (US-10)		
490 Land Securities (BR-64)	493 Nippon Yusen Kaisha (JA-93)	438 Procter & Gamble (US-10)		
491 Land Securities (BR-64)	494 Nippon Yusen Kaisha (JA-93)	439 Procter & Gamble (US-10)		
492 Land Securities (BR-64)	495 Nippon Yusen Kaisha (JA-93)	440 Procter & Gamble (US-10)		
493 Land Securities (BR-64)	496 Nippon Yusen Kaisha (JA-93)	441 Procter & Gamble (US-10)		
494 Land Securities (BR-64)	497 Nippon Yusen Kaisha (JA-93)	442 Procter & Gamble (US-10)		
495 Land Securities (BR-64)	498 Nippon Yusen Kaisha (JA-93)	443 Procter & Gamble (US-10)		
496 Land Securities (BR-64)	499 Nippon Yusen Kaisha (JA-93)	444 Procter & Gamble (US-10)		
497 Land Securities (BR-64)	500 Nippon Yusen Kaisha (JA-93)	445 Procter & Gamble (US-10)		
498 Land Securities (BR-64)	501 Nippon Yusen Kaisha (JA-93)	446 Procter & Gamble (US-10)		
499 Land Securities (BR-64)	502 Nippon Yusen Kaisha (JA-93)	447 Procter & Gamble (US-10)		
500 Land Securities (BR-64)	503 Nippon Yusen Kaisha (JA-93)	448 Procter & Gamble (US-10)		
501 Land Securities (BR-64)	504 Nippon Yusen Kaisha (JA-93)	449 Procter & Gamble (US-10)		
502 Land Securities (BR-64)	505 Nippon Yusen Kaisha (JA-93)	450 Procter & Gamble (US-10)		
503 Land Securities (BR-64)	506 Nippon Yusen Kaisha (JA-93)	451 Procter & Gamble (US-10)		
504 Land Securities (BR-64)	507 Nippon Yusen Kaisha (JA-93)	452 Procter & Gamble (US-10)		
505 Land Securities (BR-64)	508 Nippon Yusen Kaisha (JA-93)	453 Procter & Gamble (US-10)		
506 Land Securities (BR-64)	509 Nippon Yusen Kaisha (JA-93)	454 Procter & Gamble (US-10)		
507 Land Securities (BR-64)	510 Nippon Yusen Kaisha (JA-93)	455 Procter & Gamble (US-10)		
508 Land Securities (BR-64)	511 Nippon Yusen Kaisha (JA-93)	456 Procter & Gamble (US-10)		
509 Land Securities (BR-64)	512 Nippon Yusen Kaisha (JA-93)	457 Procter & Gamble (US-10)		
510 Land Securities (BR-64)	513 Nippon Yusen Kaisha (JA-93)	458 Procter & Gamble (US-10)		

Was it a *midlife* crisis?



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YOUNG TIGER

As Indonesia develops, its stocks are pulling investors from Hong Kong, Singapore, and Thailand

omy that was long Asia's laggard. And Mexico, sticking to its reform course through the peso crisis, appears to be growing again.

After two years of slogging, many emerging economies are back on track. For companies in the BUSINESS WEEK ranking compiled by Morgan Stanley Capital International Inc., total market value at the end of May rose to \$858 billion, up 16.3% from \$738 billion 18 months earlier. This year, for the first time, MSCI has provided a broad range of new in-

formation for each company including sales, profits, price/earnings ratios, and asset values. Market value is calculated by multiplying the share price times the total number of shares outstanding, including those held by governments.

Again this year, Korean heavyweights dominate the rankings by several basic measures. While Korea Electric Power kept its grip as No. 1 in market value, Samsung Electronics led the ranking both in sales, totaling \$20.5 billion, and profits, with \$3.2 billion. The runner-up in sales was Brazil's state-run oil company Petrobrás, but the rest of the top five revenue producers were Korean: Hyundai Motor, Korea Electric, and Pohang Iron & Steel.

In return on equity, Rothmans of Paterson (Malaysia), No. 108, swept the field with an astonishing 164%. The highly profitable company paid out a special dividend to stockholders from the huge cash reserves it had piled up. Asia's semiconductor boom placed three companies in the top five—Taiwan Semiconductor, Samsung Electronics, and Taiwan's United Microelectronics—with returns between 42% and 53%.

Apart from companies' individual performances, share prices and market values have been fueled by rising confidence among local and foreign investors. Another measure of emerging-market health, the stock price index of the International Finance Corp. (IFC), climbed 10% this year through mid-June. Big gains included 37% for companies in India, 29% for Taiwan, and 16% for Brazil.

"My theory is that the U.S. market

REFORMS ARE BEARING FRUIT

After two tough years, emerging markets are back

For a spectacular corporate leap forward, it would be hard to match the performance of Kimberly-Clark de México. The paper products maker, 46% owned by Dallas-based Kimberly-Clark Corp., jumped from No. 132 in 1995 to No. 48 this year on BUSINESS WEEK's annual scoreboard of the top 200 emerging-market companies, ranked by market value. Despite Mexico's recession, its share price zoomed 78%, to \$18, reflecting the company's success in gaining market share and expected benefits from its planned merger with Scott Paper Co.'s Mexican unit.

On the Pacific's other rim, the Philippines is Asia's rising economic star. Riding its strong growth, earnings of Manila Electric Co., No. 74, rose to \$168 million in 1995, up 29% from 1994. Earn-

ings should rise an additional 18% this year, says Nigel Webber, portfolio manager for Crosby Asset Management in Hong Kong. "It's a good proxy for the Philippines economy," says Cristina Lam, a director of portfolio management at Crosby.

NEW DYNAMISM. Both companies show how important free-market reforms are to business performance in emerging markets. In the Philippines, the shift is generating new dynamism in an econ-

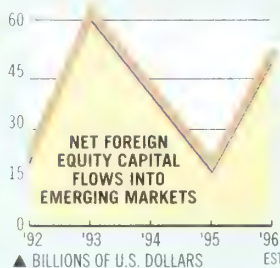
EMERGING MARKETS STALLED IN 1995...



▲ TRILLIONS OF U.S. DOLLARS

DATA: INTERNATIONAL FINANCE CORP. DATA FOR 60 EMERGING MARKETS. I NG BARINGS

...BUT INVESTMENTS ARE FLOWING IN AGAIN

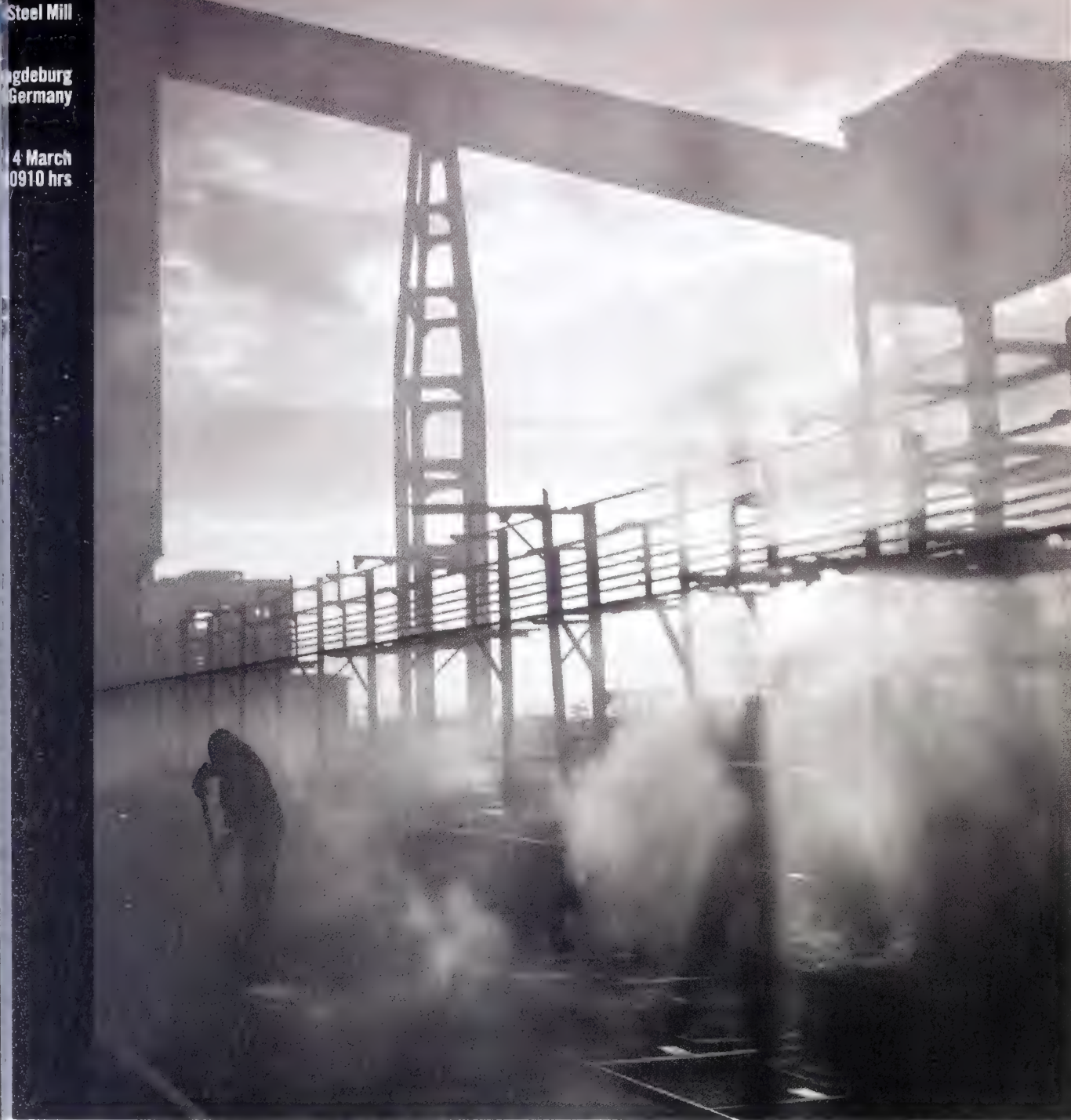


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WORLD LEADERS IN INSURANCE AND FINANCIAL SERVICES

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overpriced and very speculative," says Barton M. Biggs, head of global strategy at Morgan Stanley Asset Management Inc. Mutual-fund investors, he says, "are going to switch at the margin from the U.S., where they're not making any money, into international in general, but particularly into the area where the really high-growth and sexy stories are, which is the emerging market." Michael J. Howell, head of global investment at ING Barings, estimates the influx of foreign money into emerging-market equities will total \$50 billion this year, second only to the previous \$62 billion peak in 1993 (chart).

CHEAP STOCKS. The underlying force driving the emerging-market rallies, however, is productive gains from market reforms and corporate restructuring. As a result, says Joyce E. Cornell, lead portfolio manager for Scudder, Stevens & Clark Inc.'s Emerging Markets Growth Fund, stocks in many markets are now low-priced compared with their earnings. "You've had the deepening of political and economic reforms, and much higher earnings, at the same price," she says.

Two of the highest fliers are Indonesian cigarette makers Gudang Garam, No. 22, up 119%, and H. M. Sampoerna, No. 40, up



73%. They are cashing in on rising consumer demand in a country with 190 million people. But uncertainty about the eventual succession to President Haji Mohamed Suharto poses political risks.

Korea's companies have sagged since April because of worries the weakening Japanese yen will hurt Korea's exports and balloon its trade deficit. But a government construction boom is benefiting companies such as Hyundai Engineering & Construction Co.

In Brazil, revenues and stock prices are rising at state-controlled phone companies, including Telebrás, No. 2, and Telesp, No. 11, as rate hikes begin to pave the way toward privatization.

BIG LEAP

Booming market share and a planned merger fueled a 78% rise in the stock of Kimberly-Clark de México

Some of the most dynamic emerging-market companies are in countries new to the market-economy club. In Poland, for example, earnings gain range as high as 100%. Some of the hottest growth sectors are food, pharmaceuticals, and construction.

On June 20, the IFC announced it is adding Russia, Morocco, and Egypt to the 27 markets it tracks with daily indexes, and 14 "frontier" markets, such as Lithuania and Botswana, that it will track with monthly indexes, for a total of 44. "All of a sudden, there's a lot of activity in areas where there hadn't been much," says Robert Shakotko, the IFC's database manager.

Asian and Latin American companies may soon find themselves jostling for position on the scoreboard with upstart companies in these fledgling markets.

By John Pearson in New York, with bureau reports

The Top 100 Emerging-Market Companies

RANK 1994	RANK 1995	COMPANY	COUNTRY	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	%CHANGE FROM 1995 (U.S. \$) (LOCAL)		PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE
						1994	1995								
1	1	KOREA ELECTRIC POWER	Korea	23945	38	2	6	1.5	21	1.7	12710	1155*	34476*	7.2	12
2	9	TELEBRAS	Brazil	20740	65	93	112	0.8	15	1.5	8635	811	35753	5.1	55
3	2	TELEKOM MALAYSIA	Malaysia	18209	9	19	21	4.7	29	0.7	2102	629	5897b	16.4d	55
4	8	CATHAY LIFE INSURANCE	Taiwan	16413	6	36	47	17.7	43	0.9	NA	NA	NA	41.1	63
5	6	ANGLO AMERICAN	South Africa	15111	65	22	44	2.9	17	1.7	NA	NA	7088	16.7	81
6	3	TELEFONOS DE MEXICO (TELMEX)	Mexico	15023	2	17	41	1.6	9	2.9	5610	1249	12523	17.3	55
7	NR	PT TELEKOMUNIKASI INDONESIA	Indonesia	14205	2	NA	NA	4.4	37	0.7	2189	389	5036b	12.2	55
8	4	ELETRORAS	Brazil	13215	243	-12	-4	0.2	15	0.9	5782	758	106870	1.2	12
9	5	TENAGA NASIONAL	Malaysia	13050	4	3	4	2.4	40	0.8	2744	497	9651b	6.1d	12
10	10	DE BEERS CONSOLIDATED MINES	South Africa	12391	33	29	52	1.6	15	2.5	NA	NA	NA	10.8	26
11	30	TELECOMUNICACOES DE SAO PAULO (TELESP)	Brazil	11237	211	70	87	1.3	26	3.6	2466	302*	11333*	5.0	55
12	11	MALAYAN BANKING	Malaysia	10827	9	15	17	5.8	28	0.6	NA	346	32731	20.5	61
13	7	SAMSUNG ELECTRONICS	Korea	10172	88	-18	-15	1.4	3	1.1	20547	3180*	17211*	45.0	41
14	12	HUA NAN BANK	Taiwan	10138	5	11	21	7.4	52	0.8	NA	195*	NA	14.2	61
15	13	PETROBRAS	Brazil	10054	72	-3	6	0.4	12	1.4	15967	623	31008	3.1	11
16	14	BANGKOK BANK	Thailand	9887	10	11	14	2.7	13	2.2	NA	785	35665b	21.3	61
17	17	FIRST COMMERCIAL BANK	Taiwan	9591	5	26	36	7.1	52	0.5	NA	185*	NA	13.7	61
18	16	SOUTH AFRICAN BREWERIES	South Africa	9023	30	8	28	7.1	24	1.9	7476	381c	4265	29.8	43
19	20	CHANG HWA COMMERCIAL BANK	Taiwan	8699	5	27	38	7.1	58	0.7	NA	151*	NA	12.3	61
20	21	VALE DO RIO DOCE	Brazil	8156	21	11	22	0.8	23	1.6	3499	329	13891	3.4	25
21	NR	PETRONAS GAS	Malaysia	7853	4	NA	NA	8.1	27	0.9	486	293c	2149	30.2d	12
22	65	GUDANG GARAM	Indonesia	7837	8	119	129	10.0	50	0.6	2399	157	1530b	20.1	43
23	35	YPF	Argentina	7769	22	10	10	1.3	10	3.6	4956	793*	9141*	12.6	11
24	36	KRUNG THAI BANK	Thailand	7187	5	35	39	4.1	17	2.4	NA	402*	21984b*	23.7	61
25	28	LIBERTY LIFE ASSOCIATION OF AFRICA	South Africa	7155	29	7	27	2.4	26	2.0	2631	175b	23112b	9.6	63

a) Based on 1994 data. b) Based on 1995 data. c) Based on 1996 data. d) Difference between earnings and book value between 12 and 18 months. e) Results are for 7 months. LOSS=Negative ratio. NA=Not available. NEG=Negative return. Data: Morgan Stanley Capital International

RANK 1996	RANK 1995		COUNTRY	MARKET VALU U.S. \$ MIL	PRICE PER SHARE U.S. \$	%CHANGE FROM 1995 (U.S. \$) (LOCAL)	PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALV. U.S. \$ MIL	PROFIT U.S. \$ MIL	Assets U.S. \$ MIL	RETURN ON EQUITY %	INDUSTRY CODE	
26	NR	HELLENIC TELECOMMUNICATIONS ORGANIZATION	Greece	7022	17	NA	NA	3.2	17	3.1	1999	493b	NA	18.7	55
27	37	BANCO BRADESCO	Brazil	6915	10	38	51	1.3	11	2.9	NA	541	3292b	11.8	61
28	29	TELEFONICA DE ARGENTINA	Argentina	6910	3	9	9	2.0	16	3.5	2733	458	537b	12.7	59
29	25	CHINA STEEL	Taiwan	6904	1	1	9	1.7	34	5.6	2781	203*	NA	5.1	25
30	45	GRUPO CARSO	Mexico	6706	7	58	90	2.2	15	0.0	NA	NA	4167	14.2	71
31	19	POHANG IRON & STEEL	Korea	6459	69	-16	-13	0.8	6	1.2	10431	1066b	1690b	13.6	25
32	23	RESORTS WORLD	Malaysia	6293	6	-12	-11	7.9	29	1.0	747	219	1027b	27.5d	53
33	31	SIME DARBY	Malaysia	6229	3	-6	-4	3.0	23	2.4	3760	228	3601	12.9	71
34	NR	SHIN KONG LIFE INSURANCE	Taiwan	6104	4	NA	NA	7.5	31	1.3	NA	NA	NA	24.3	63
35	32	THAI FARMERS BANK	Thailand	6067	8	4	7	2.9	13	2.8	NA	457*	20094b*	21.9	61
36	34	SASOL	South Africa	5989	10	8	28	2.6	12	2.5	2742	428	3904	21.5	22
37	20	GENTING	Malaysia	5967	8	-20	-18	5.0	28	0.7	999	213	2024b	17.7d	53
38	NR	PAKISTAN TELECOMMUNICATIONS	Pakistan	5936	1	NA	NA	3.6	12	2.2	950	484*	NA	29.2	55
39	22	SIAM CEMENT	Thailand	5820	49	-19	-17	5.3	23	1.6	3244	239	3774b	23.6	21
40	78	HM SAMPOERNA	Indonesia	5590	12	73	82	15.3	37	0.7	715	151	NA	41.4d	43
41	76	KOREA MOBILE TELECOM.	Korea	5521	963	63	69	6.1	24	0.1	1678	230*	352b	25.5	56
42	41	GENCOR	South Africa	5413	4	22	44	2.5	19	1.2	NA	NA	2148	12.8	81
43	56	AYALA	Philippines	5315	1	26	28	5.6	19	0.2	NA	NA	1648b	29.3d	71
44	NR	TAIWAN SEMICONDUCTOR MFG.	Taiwan	5288	2	NA	NA	4.4	8	0.0	1039	545	NA	53.2	34
45	66	UNITED ENGINEERS (MALAYSIA)	Malaysia	5223	7	5	7	7.5	35	0.3	724	108	1246b	21.0d	71
46	40	INTERNATIONAL COMMERCIAL BANK OF CHINA	Taiwan	5131	3	15	24	5.3	39	0.4	NA	111b*	NA	13.5	61
47	27	ENDESA	Chile	5083	1	-26	-19	1.9	14	7.2	859	371	5234	13.3	12
48	132	KIMBERLY-CLARK DE MEXICO	Mexico	5038	18	78	114	5.0	23	2.2	926	152	1222	21.2	45
49	18	COPEC	Chile	4994	4	-34	-29	1.5	13	2.5	2825	427	3911b	11.9	11
50	15	TELECOMASIA	Thailand	4873	2	-42	-41	3.5	130	0.0	189	51	2221b	2.7d	55
51	72	BANCO ITAU	Brazil	4837	405	45	60	1.4	11	1.6	NA	375	NA	12.3	61
52	84	PEREZ COMPANC	Argentina	4818	6	68	68	3.1	17	1.7	1468	241	2832	17.8	71
53	100	GRUPO TELEVISIA	Mexico	4770	15	89	128	4.1	92	0.0	1186	127	2616	4.4	51
54	50	CIFRA	Mexico	4755	1	18	42	2.8	23	0.0	2708	708	1762	12.1	54
55	54	REMBRANDT GROUP	South Africa	4639	9	22	45	2.4	16	1.6	NA	NA	2240	15.7	43
56	77	PTT EXPLORATION & PRODUCTION	Thailand	4628	15	42	45	10.0	123	0.3	144	24b	775b	8.2	11
57	52	COMPANIA PERUANA DE TELEFONOS	Peru	4627	2	15	24	3.6	15	1.1	991	292	1397b	23.8d	55
58	36	TELECOM ARGENTINA STET-FRANCE TELECOM	Argentina	4589	5	-6	-6	2.0	16	4.6	1933	307*	4651*	12.5	55
59	NR	PORTUGAL TELECOM	Portugal	4579	24	NA	NA	2.0	20	2.4	2574	230	5618b	10.2	55
60	33	SAN MIGUEL	Philippines	4577	2	-29	-28	3.1	19	1.7	3024	205	2757b	16.6d	43
61	74	CEMEX	Mexico	4564	4	23	48	1.1	5	2.3	2661	788	7128	24.2	21
62	39	TELECOMUNICACIONES DE CHILE (CTC)	Chile	4502	5	1	9	2.5	16	3.4	1033	267	3646	16.2	55
63	75	SIAM COMMERCIAL BANK	Thailand	4475	17	36	39	3.2	15	2.3	NA	306*	NA	22.0	61
64	46	STANDARD BANK INVESTMENT	South Africa	4373	36	3	22	2.9	15	2.1	NA	289	NA	19.3	61
65	106	METROPOLITAN BANK & TRUST (METROBANK)	Philippines	4355	30	57	60	5.6	29	0.5	NA	134	NA	19.3d	61
66	42	INDOCEMENT TUNGGAL PRAKARSA	Indonesia	4296	4	-3	1	3.9	21	1.4	1690	204	2382b	18.6	21
67	117	CERVEJARIA BRAHMA	Brazil	4172	597	75	92	4.0	15	1.5	2244	251	NA	27.5	43
68	47	CHINA DEVELOPMENT	Taiwan	4135	3	-1	7	4.5	26	0.0	NA	108b*	NA	17.4	62
69	63	ADVANCED INFO SERVICE	Thailand	3937	17	9	12	11.9	30	1.2	393	118	606b	40.1	55
70	43	NAN YA PLASTICS	Taiwan	3936	2	-11	-3	2.8	14	2.6	3823	290	NA	20.8d	22
71	NR	GRUPO MODELO	Mexico	3868	5	NA	NA	2.4	32	0.5	1317	112*	NA	7.7	43
72	62	ENERGIS	Chile	3851	1	6	6	2.6	16	4.9	1803	239	3735	16.4	12
73	NR	STATE BANK OF INDIA	India	3802	8	NA	NA	2.8	21	1.2	NA	204*	NA	13.5	61
74	59	MANILA ELECTRIC	Philippines	3784	6	-11	-10	2.8	17	1.6	1752	168	1613b	16.1d	12
75	NR	MAHANAGAR TELEPHONE NIGAM	India	3730	1	NA	NA	6.1	19	0.5	851	165*	NA	31.9	55
76	38	DAEWOO HEAVY INDUSTRIES	Korea	3723	10	-22	-19	1.1	23	3.1	5030	164	8904b	4.7	38
77	44	UNITED MICROELECTRONICS	Taiwan	3636	1	-18	-12	3.2	7	0.9	876	486	NA	42.2	35
78	69	LIBERTY HOLDINGS	South Africa	3603	75	2	20	2.1	22	2.2	NA	NA	23217b	9.9	63
79	57	TATUNG	Taiwan	3595	2	-3	5	3.2	14	1.2	2343	227b	NA	23.3	71
80	104	GRUPO FINANCIERO BANACCI	Mexico	3571	2	38	67	1.7	4	0.0	NA	817	1999	40.9	61
81	49	INDOSAT	Indonesia	3563	3	12	8	4.4	18	1.7	448	197	698b	24.6	55
82	61	FORMOSA PLASTICS	Taiwan	3524	1	-3	5	3.0	19	2.3	1309	197	NA	16.0d	55
83	73	INDOFOOD SUKSES MAKMUR	Indonesia	3459	4	4	9	5.9	26	0.5	896	131	616b	22.2	44
84	85	CEMIG	Brazil	3440	27	15	27	0.4	15	3.8	1646	217*	11557*	2.5	12
85	70	LIGHT-SERVICOS DE ELETRICIDADE	Brazil	3415	329	0	10	1.1	-73	0.7	1468	-110*	4194*	NEG	12
86	92	ANGLO AMERICAN INVESTMENT TRUST	South Africa	3383	34	24	48	2.6	14	3.1	NA	NA	1195b	19.1	26
87	NR	VIDESH SANCHAR NIGAM	India	3369	42	NA	NA	12.5	32	0.2	1016	85*	NA	38.5	55
88	105	TATA ENGINEERING & LOCOMOTIVE	India	3350	14	23	37	7.5	25	0.8	1619	91*	1217*	30.5	42
89	67	UNITED COMMUNICATION INDUSTRY	Thailand	3308	14	-7	-4	4.5	30	0.9	541	111	763b	15.1	55
90	58	SHINAWATRA COMPUTER & COMMUNICATIONS	Thailand	3306	24	-10	-8	10.5	25	1.2	547	65b	1201b	41.5	34
91	97	HINDUSTAN LEVER	India	3279	22	20	34	18.2	48	1.3	961	68*	472b*	37.9	44
92	82	RELIANCE INDUSTRIES	India	3209	7	21	-12	1.5	8	2.5	2223	373c*	3291*	18.1d	22
93	94	GOLD FIELDS OF SOUTH AFRICA	South Africa	3181	33	21	43	5.2	40	1.5	NA	NA	689	13.0	81
94	NR	STEEL AUTHORITY OF INDIA	India	3176	1	NA	NA	1.6	8	2.2	4319	379c*	NA	19.2d	25
95	55	PHILIPPINE LONG DISTANCE TELEPHONE	Philippines	3102	58	-19	-18	1.8	20	0.4	964	144	3142b	9.0d	55
96	89	MALAYSIAN INTERNATIONAL SHIPPING	Malaysia	3082	3	12	13	1.9	14	2.6	991	225	1972b	13.7d	58
97	48	PETRON	Philippines	3058	0	-26	-25	6.5	19	2.3	1705	154	1294b	33.4d	11
98	87	DRIEFONTEIN CONSOLIDATED	South Africa	2994	15	7	27	3.9	62	2.8	583	103	936	6.4	81
99	111	NEDCOR	South Africa	2976	14	16	37	2.7	14	2.1	NA	179	NA	18.4	61
100	131	AMALGAMATED BANKS OF SOUTH AFRICA	South Africa	2973	5	38	64	1.9	11	2.7	NA	259c	NA	17.0	62

LET'S GET GROWING

The economy can run faster. Here's how to make it happen

Can America grow faster? Right now, that may seem like an odd question. Employment is surging, the stock market is strong, and corporate profits are up. In the second quarter, economic growth could top a 4% annual rate.

But hardly anyone expects the current spurt to last much longer. Forecasters predict that the economy will soon revert to an average annual growth rate of 2% or so, continuing the long growth slide that began in the mid-1970s. In fact, growth since 1990 has averaged only 1.9%.

Cover Story

Such lukewarm gains aggravate virtually every economic and

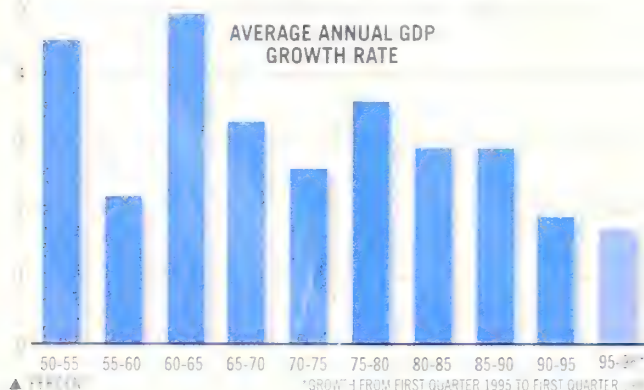
social problem that plagues the country. Slow growth means stagnant wages, slipping standards of living, and insecure jobs. Americans feel as if they're scraping by: It's hard for families to save for retirement, it's hard for governments to pay for essential services, it's hard for corporations to expand.

Raising the long-term growth rate by just one percentage point, from 2% to 3%, could produce a massive payoff in wages, living standards, and economic security. As a result, a vigorous new growth debate has sprung up, fueled in part by

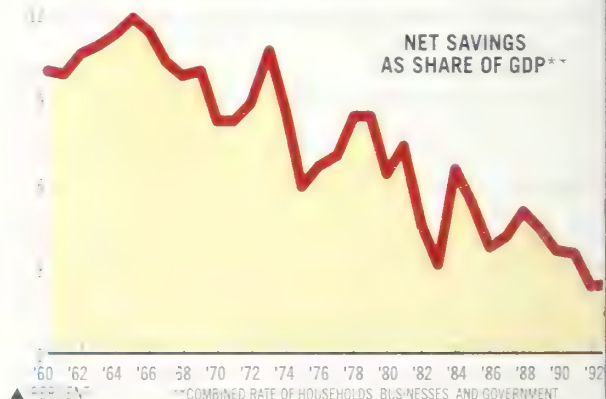
election-year politics. There are those who regard 2% to 2.5% growth as if it were some iron law of nature. For instance, some members of the Federal Reserve, joined by a Cassandra-like chorus of bond-market vigilantes, fear that any attempt to boost growth above that rate will only reignite inflation. But many business leaders disagree, saying the U.S. could enjoy an economic boom if only the Fed would ease off the brakes. Republican Presidential candidate Bob Dole says the economy could double its growth rate with big tax cuts—but that would likely increase the deficit. President Clinton responds that the economy is doing quite nicely on his watch—but he, too, is prepared to stimulate growth with a set of budget-busting handouts.

The truth is, this economy can achieve faster growth without higher inflation—but not by resorting to quick fixes or trendy tax plans. Instead, the U.S. must attack its twin fundamental problems: too little savings and too little investment. Net national savings—the funds available for new investment—average less than 5% of the nation's output, down from the 11% average of the 1960s, when the economy zipped along at a 4% average annual pace. And despite massive spending on computers and other technical gear, business investment is barely keeping ahead of depreciation on existing plant and equipment. As a result, net business investment is languishing at an astonishingly low 2% of GDP (chart).

THE SYMPTOM: SLOW GROWTH



THE CAUSES: NOT ENOUGH SAVING



That's why BUSINESS WEEK believes the U.S. has to go back to economic basics: It must save more so it can invest more in new machines, new technologies, and better-educated workers. Increased savings will lower interest rates and cut the cost of capital. Cheaper funds will encourage investment, which will fuel stronger growth without higher inflation. It's simple, says Boston University economist Laurence J. Kotlikoff. "Countries that don't save, don't invest—and countries that don't invest, don't grow."

QUICK RESPONSE. Shifting to pro-savings, pro-investment economic policy can lift the economy over the next few years to a long-term growth rate of 3% or more. The payoff from such an acceleration would be enormous. A decade from now, the economy would produce an extra 3,000 in goods and services for every American adult and child. In 30 years, faster growth would add 35% to economic output, assuring comfortable retirements for baby boomers.

A pro-savings, pro-investment policy is the most direct way to boost the country's competitiveness in international markets. With more and newer machines and equipment, U.S. workers would be more productive. And higher levels of investment would also enable companies to more quickly adopt new technologies.

BUSINESS WEEK's growth plan will require three major changes in government policy. To begin with, the next President and Congress must remove Washington's rain on saving by balancing the budget. How? Not by raising taxes, as President Bush did in 1990 or President Clinton did in 1993, but

by cutting spending. Putting the budget on a five- to eight-year path toward balance would lower long-term interest rates by almost two percentage points and make it easier for businesses to get the funds they need to invest.

Second, the tax system needs to be overhauled and simplified. The goal is to let capital flow freely to the investments with the best economic return. That doesn't mean taking the radical step of shifting to a flat tax. Instead,

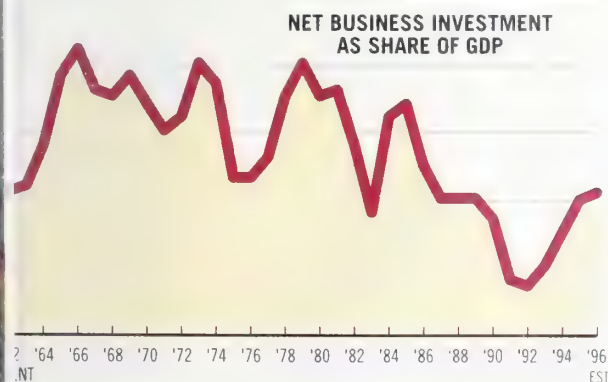
BUSINESS WEEK advocates closing tax loopholes that distort investment and savings decisions. The resulting savings would pay for a tax cut to bring individual rates back to or below the 28% top bracket of 1986, from today's top rate of about 40%.

The third, and most controversial, step: Convert Social Security to a fully funded pension system, complete with individual savings accounts. Privatizing Social Security would boost national savings and increase U.S. plant and equipment by 25% by 2020. The massive flow of funds into the equity markets would substantially reduce the cost of capital and encourage investment. Sure, the shift to a privatized system would force workers to bear more risks. But far more menacing are the threat of slow growth and the danger of a breakdown in the current Social Security system.

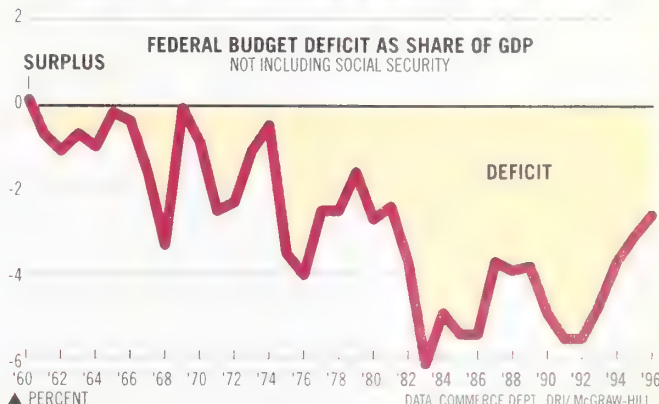
Other changes are needed as well. Along with more investment and savings, the economy needs better-educated workers. Indeed, the return on investment in human capital is higher than the payoff on physical capital: Economists estimate that spending on education yields 10% to 15% annual returns,

Individuals and businesses
are saving far less than they
did 30 years ago—and the cost
of capital has soared

...LOW INVESTMENT...



...AND A STUBBORN BUDGET DEFICIT



after inflation. Ideas to reform schools and ease access to higher education are crucial to the economy's long-term growth.

But even the best-educated worker cannot succeed without the right equipment. Americans simply aren't saving enough to support the growth

Cover Story

they want. Individuals and businesses alike are saving far less of their income than they did 30 years ago, thanks to a societal shift away from thrift and toward financial innovations that allow more debt.

One clear result: Capital costs are a lot higher than in the fast-growth '60s. In that decade, when inflation averaged 2.5% a year, triple-A corporate borrowers could issue long-term bonds at 5%, a real interest rate of 2.5%. In the 1990s, average inflation is only slightly higher, at 3.3%, but corporate rates have averaged 8.2%—a real rate of almost 5%.

DEFICIT DRAIN. With the increasing integration of the global economy, some analysts argue that domestic savings don't matter. The trillions of dollars that move through foreign exchange markets create an immense river of capital, ready to flow to the economy that offers the highest returns. In theory, a low-savings country such as the U.S. can finance its growth by borrowing from Japanese or European savers. To some extent, that's what has been happening. The U.S. financed its 1980s consumption spree in part by borrowing from abroad.

But global capital markets haven't broken the link between a country's savings and its ability to invest. "Maybe one-third of the world's capital is in the global pool—the rest stays home," says Stanford University economist Paul R. Krugman. So economies with high savings rates, such as Japan, Korea, and Taiwan, maintain much higher investment rates over long periods than low-savings countries such as Britain, Canada, Sweden—and the U.S. High savings don't wipe out the business cycle: The Japanese, who still tuck away 13% of their income, have suffered through a four-year recession. But as the Japanese boom of the '80s demonstrated, savings can power strong growth.

Even if more foreign capital were available, borrowing from abroad to finance investment at home is a losing proposition. Although the dollar is gaining strength now, foreign investors still demand an interest-rate premium to protect themselves from the risk of exchange rate losses. And like any loans, foreign borrowings must be repaid with interest. By the end of 1994, the latest data available, Americans had borrowed so much abroad that they owed a net \$584 billion to foreigners. The result: "We're sending a growing share of the

fruits of our labors to foreigners, instead of using them to improve our own living standards," says Harvard University economist Benjamin Friedman.

Raising the capital for faster growth at home has its price. To save more, Americans must consume less—and that includes the government. Federal deficits, not including Social Security, have risen from their 1960s' average of 0.9% of gross domestic product to 4.2% in the 1990s. Even with the deficit coming down from its peak, Washington still consumes more than a third of a meager pool of private savings. "We've tried all kinds of tax

breaks and other things to boost savings, with no result," says Martha Phillips, executive director of the antideficit Concord Coalition. "The only thing we know will work is to balance the budget."

That's not just some arcane economic theory. In 1993, the passage of deficit-cutting legislation triggered a bond rally that cut interest rates 1.4 percentage points in 10 months. Over the long run, a credible plan to eliminate the budget deficit could, by itself, give the economy a one-time boost of 0.8% of GDP and raise the long-term growth rate by one-quarter of a point, according to DRI/McGraw-Hill estimates.

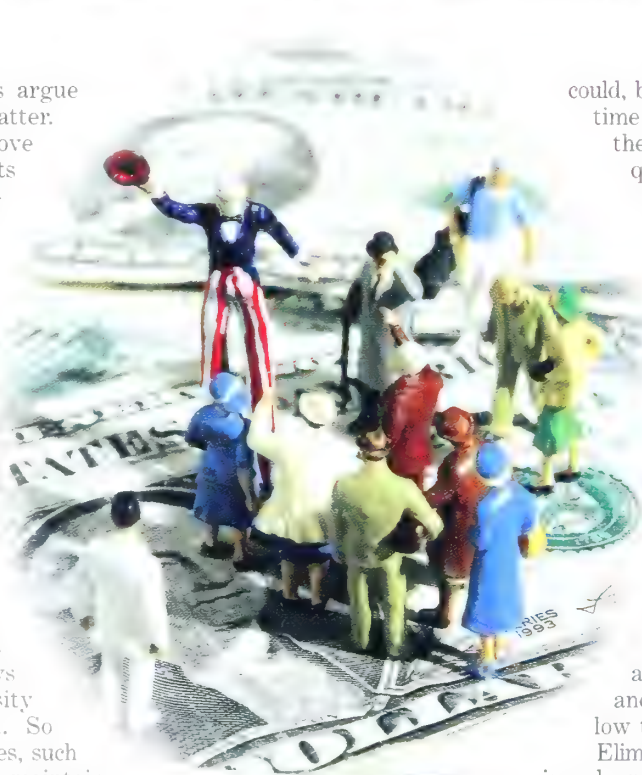
TAX ROULETTE. How should the goal of a balanced budget be reached? Earlier this year the Republicans and the Democrats came within an eyelash of agreeing on a deal to balance the federal budget by 2002 solely through spending cuts. That deal broke down—a historic opportunity lost to political posturing. Any plan to cut the deficit should follow similar lines. That means slowing the 9% annual increases in Medicare and Medicaid spending, while holding the already slow growth in defense and other domestic spending below the rate of inflation.

Eliminating the deficit, while essential, is only part of the growth prescription.

The U.S. also needs a streamlined tax system. A new tax code must lower rates and eliminate distortions that punish savings and investment. With a few exceptions for clear social goals, such as encouraging homeownership and charitable giving, reformers must wipe out subsidies and special tax breaks that turn business decisions into tax roulette.

This doesn't mean massive tax cuts or a shift to a radically new tax system. While such calls may win applause on the hustings, neither will guarantee a prosperous 21st century. Look at the precedent: Ronald Reagan's massive

Privatizing Social Security would, over time, be the biggest boost to growth and would help create more of a savings culture



HOW THE U.S. ECONOMY STACKS UP

1996 ESTIMATES

■ U.S.
■ JAPAN
■ GERMANY

SOURCE: DRI/McGraw-Hill

ix cut of 1981 didn't produce any surge
savings or investment.

Moreover, studies suggest that a new
ystem that taxes consumption and ex-
mpts savings—such as the 17% flat tax
umpeted by Steve Forbes in the GOP
rimaries—could at best enlarge the econ-
ny by a meager 4% after a decade, says
niversity of California at Berkeley econ-
nist Alan J. Auerbach. Even this effect
ould be further diluted by adding in
w-rate brackets to ease the burden on
ie poor and special benefits to ease busi-
ness' switch to a new code.

BEHAVIOR CHANGE. A better idea is an
erhaul rather than a replacement. Con-
gress and the White House should strive
improve upon the Tax Reform Act of
1986, which closed loopholes and shut
own tax shelters to fund a sharp reduc-
on in tax rates. The goal should be to
all rates down to or below the 1986
rackets of 15% and 28%.

That will require eliminating a host of
pecial-interest tax breaks. Many such
its will hit specific industries—such as fi-
ancial services (\$12 billion in annual tax
eaks), energy (\$2.5 billion), and mining
1.5 billion). But Congress should look
urd at tax breaks that favor individuals,
o. While the deduction for mortgage
terest helps support homeownership,
ie cap on such deductions could be sig-
ificantly reduced: Anyone who can afford a \$1 million mort-
age can get by without full deductibility. Congress should
so look again at interest deductions for home-equity loans,
3% of which fund car purchases or other consumption, not
me improvements or other investments.

A tax overhaul should also put to an end the bickering
er how to tax capital gains. The right approach: Tax gains
st like other types of investment income, such as interest
d dividends. Giving special tax breaks to capital gains can
stort investment decisions. Moreover, after years of wran-
ing, economists can produce little clear evidence that lower
tes on gains boost the investment in equipment and human
pital that the economy needs to grow. Instead, much of the
lvantage from a lower rate on gains goes to buyers and sell-
s of real estate. The revenue that would be lost by giving
eferential treatment to capital gains could better be applied
lowering rates for all taxpayers.

Cleaning up the tax code will help ensure that invest-
ent follows market forces, not political dictates. And a sim-
er code with fewer deductions and lower rates will reduce

THE GROWTH PRESCRIPTION

*For faster growth, Americans must
save more and invest more. Here's
how:*

■ **BALANCE THE BUDGET** Wash-
ington siphons away more than one-
third of a shrinking pool of private
savings. Balancing the budget will
cut the cost of capital to business.
Interest rates would fall by almost
two percentage points, igniting a
much needed investment boom.

■ **OVERHAUL TAXES** A simpler,
clearer tax system can cut the cost
of compliance with today's code.
Rates can be cut back to the 1986
brackets—15% and 28%—by elimi-
nating industry-specific tax breaks
and reining in overgrown personal
deductions. The result: Funds will
flow to the most economically sound
investments.

■ PRIVATIZE SOCIAL SECURITY

Today's pay-as-you-go retirement sys-
tem is a drain on savings—and is
headed for breakdown. Diverting
part of the payroll tax into private
retirement accounts will create a
healthy mix: rapidly growing savings
accounts backed by a social-insur-
ance safety net for the disabled, sur-
vivors, and low-wage workers.
Switching to private accounts will
require financing Social Security's \$8
trillion to \$12 trillion in unfunded
promises—a transition cost that
must be shared by all generations,
including current retirees. But the
payoff will be higher savings and
faster growth. And what's more, it
will mean a secure retirement for
future generations, a scenario that is
becoming less likely under the cur-
rent system.

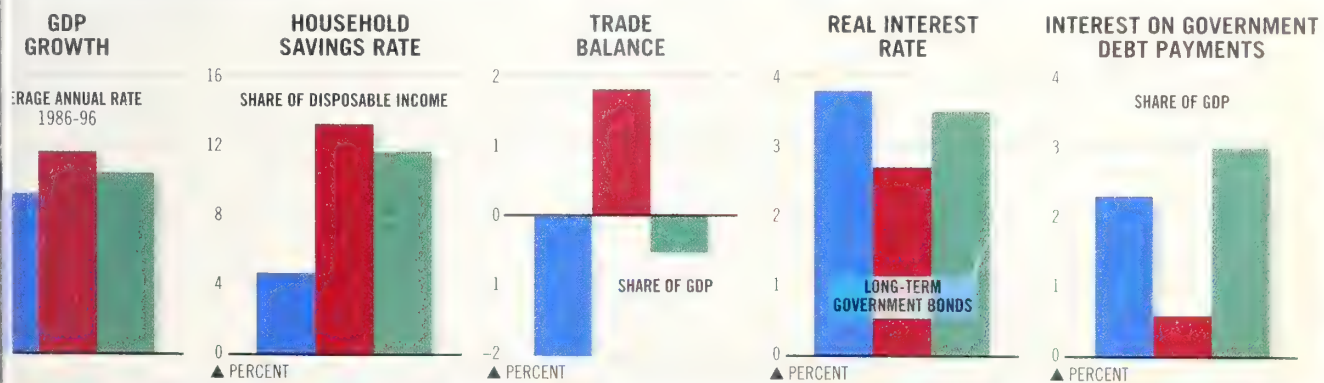
the compliance burden. By freeing up more money to boost
savings and investment, a revamping of the tax code could
quickly pay dividends in terms of improved growth.

In the long run, though, the single biggest boost to savings
and growth will come from privatizing Social Security—con-
verting it to a combination of social insurance and worker-
owned investment accounts. This dramatic change is the best
opportunity to create more of a savings culture in the U.S.

BUSINESS WEEK's plan for boosting growth would break
Social Security into three parts, following a proposal by five
members of the President's Advisory Council on Social Se-
curity. Each part would be funded by a share of the existing
12.4% payroll tax now paid by workers and employers.

The first part would be a standard pension for all workers,
supported by a 5% payroll tax. Second would be survivors'
and disability insurance, run by the government just as it is
now and financed by a 2.4% payroll tax. These would com-
prise the safety net.

The last five points of payroll would fund Personal Security
Accounts (PSAs)—individual accounts that workers could in-





American Airlines Interactive Travel Network

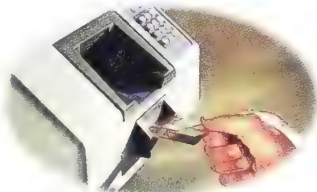
The Future Of Travel



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vest in stocks, bonds, or other approved investments. In effect, these would be defined-contribution retirement accounts, much like today's 401(k) accounts. The new system would be phased in over some 70 years. Today's retirees and workers aged 55 or over would collect benefits under the current Social Security plan.

Cover Story

get credit for their earnings in the old system, as well as the proceeds of their PSA accounts. Twentysomething workers and future generations would be wholly in the new plan.

Shifting to such a combined system would spur savings and economic growth. Fully funding Social Security will boost savings within the system, argues Harvard economist Martin S. Feldstein: Obligations owed to current beneficiaries will shrink as they age and die, while higher returns will help workers' private accounts grow faster. Feldstein estimates that the switch will bring the cost of capital down by 1.4 to 2 percentage points. Feldstein and Boston University's Kotlikoff both conclude that privatization will add 0.5 percentage points to the economy's growth rate over the next 25 years.

At the same time, privatization could help restore "an attitude that we've got to put something aside for tomorrow instead of just living for today," says Kotlikoff. Savings behavior can be changed, as employers have shown when they vigorously promote their 401(k) retirement plans. By focusing on the need for fully funding the retirement of today's and future workers, Americans might actually be induced to save more, something that they are not doing now. Baby boomers, especially, are saving only one-third of what they'll need to retire in reasonable comfort, says Stanford University economist B. Douglas Bernheim.

RISK AND REWARD. Privatization will benefit workers in another important way. Currently, payments into the Social Security trust funds earn the equivalent of about 2% annually, after inflation. That's far below the 7% average real return seen on stock market investments over the past 70 years. Under privatization, if account holders get market returns on their funds, Social Security's actuaries calculate that PSA balances will total \$14.7 trillion by 2020 and \$118.3 trillion by 2045. By contrast, the latest projections show the current Social Security trust fund peaking at \$3 trillion in 2018—and falling to zero by 2029.

Any such wholesale switch will force retirees and workers to accept more risks. Today's Social Security is immune to personal imprudence—no one can take Social Security bene-

fits in a lump sum and blow them on a bad investment. It is indifferent to the ups and downs of the financial markets. And it offers what economists call insurance against longevity because a retiree can't outlive his or her benefits.

The PSA privatization plan advocated by BUSINESS WEEK would keep some of the safety-net features of Social Security. Disability and survivors' insurance would still be retained. But privatization asks workers and retirees to assume greater risks. In most cases, the dangers can be minimized—and the rewards will outweigh the risks.

Take financial risk. Private accounts invested in stocks and bonds would be vulnerable to crashes or bear markets—raising the specter of 65-year-old workers seeing their accounts decimated just before retirement. But the fear flies in the face of the stock market record. Since the end of World War I, the return on equities has beaten Social Security's 2% inflation-adjusted return in almost every 20-year period.

Going further back, of course, the crash of 1929 and the ensuing depression wreaked havoc on stockholders. But another Great Depression would force government to step up income support in any case. **FRAGILITY.** Minimizing other risks may require strict regulations. Workers may be required to keep their Social Security savings in trust accounts with approved investments—publicly traded stocks, bond mutual funds, and other securities, and perhaps some regulated real estate partnerships—to ensure that retirees don't sink their mandated savings into speculative franchises or collectibles. To provide longevity insurance, lump-sum distributions may be banned, or retirees might be required to

put some of their funds into long-lived annuities. Even with such protections, government might have to provide a safety net. "When the debate heats up, you're going to hear a lot about the poor elderly widow who outlives her savings," warns Massachusetts Institute of Technology economist Peter A. Diamond.

Privatization may pose risks—but today's Social Security is already resting on a fragile foundation. "If we

keep going as we are, we're gambling that the whole system won't collapse or be repudiated by future generations," warns Sylvester J. Schieber, vice-president for research at benefit consultant Watson Wyatt Worldwide in Washington and one of the main advocates of the PSA. "The current system runs on political capital—the promise that the government will take workers hard enough to keep paying your benefits." The PSA plan "would replace that with real capital."

Perhaps the biggest unanswered question is how to pay for the enormous transition costs of moving to a privatized



Despite big outlays for computers, business spending on new equipment is barely keeping ahead of depreciation

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system. Right now, the benefits promised to future retirees far exceed the amount of money available from the Social Security trust funds. This shortfall is enormous: Social Security's unfunded promises to future retirees are worth \$8 trillion to \$12 trillion. Privatizing Social Security and converting it to a fully funded pension system will force the government to recognize and somehow pay for this unfunded liability.

Cover Story

Recognize and somehow pay for this unfunded liability.

Paying for the transition—and deciding which generations will bear the burden—will pose an enormous political challenge. The clout of elderly voters is already locking many politicians into a defensive stance. "We will have a lot of people running for Congress in November on the promise of saving Social Security as it is now constituted," warns Charles P. Blauhaus III, an aide to privatization advocate Senator Alan K. Simpson (R-Wyo.). And it's not just congressional candidates: During the GOP primaries, Dole lambasted rival Forbes for proposing privatization.

FED FACTOR. Nevertheless, the burden of transition must be shared across generations, by current retirees as well as current and future workers. To finance the switch to a private system, the government could issue new bonds, serviced by a 1% additional payroll tax. Such taxes would hit current and future workers—who will get a poorer return from Social Security than today's beneficiaries. To compensate, the elderly can contribute by accepting lower cost-of-living increases or higher taxes on their benefits.

Are the massive changes in policy proposed by BUSINESS WEEK really needed? Some business leaders and analysts would say they're not. These growth optimists see signs in the current economy that the long growth slide may be ending. They point to three years of double-digit growth in capital spending coupled with downsizing and heavy investment in new technologies. As a result, many U.S. businesses see rising productivity in their operations.

Moreover, the 1990s restructuring of U.S. business could be producing payoffs in quality and service that can't be captured in official statistics. So far, statisticians poring over the economy's indicators can't find a lasting increase in the 1.1% annual rate of productivity growth that has prevailed since 1973. But soaring profits and surging stock prices may be a better indication of the economy's vigor than the sluggish pace of GDP and productivity figures.

That's why many executives claim that growth could surge if policymakers, especially the Federal Reserve, would just loosen the economy's reins. The National Association of Man-

ufacturers (NAM) launched a public campaign on June 26 to urge the Fed to cut interest rates by half a percentage point and boost growth to 3%. "The Fed and the Administration should take risks on the side of growth," argues Dana C. Mead, CEO of Tenneco Inc. and chairman of NAM.

But the economy's recent performance does not suggest that the Fed has been holding back the economy. Indeed, for the past 18 months, unemployment has been below the 6% that the central bank's statisticians once calculated would ignite inflation.

Even if the Fed had its foot on the economy's brake, a tap on the accelerator wouldn't help long-term growth. Suppose the central bank could push down the unemployment rate by a further half-point, to around 5%, without accelerating inflation. The

result, says Stanford's Krugman, is that "we'd get on year of 3.2% growth—that's all. The next year, we'd be back at 2.2%. It wouldn't help the trend a bit."

NEW SPIRIT. In addition, the apparently high rate of business investment cited by the growth optimists overestimates the amount of productivity-enhancing capital actually being added to the nation's economy. Much of the new spending is on computers, which become obsolete within a few short years. To keep up with this rapid rate of depreciation, business investment needs to be far higher to actually get the useful capital stock growing quickly again.

The U.S. can't afford to wait for an uncertain boom. Even if growth is stronger than we think, the economy can still use more saving and investment. If anything, a faster-paced, higher-tech economy will increase the demand for funds. Research spending, on the decline in both federal labs and private industry, depends on a stronger stream of capital. So does the process of getting research and development out of labs and onto the production line.

"Capital investment speeds up the spread of technologies," says Berkeley economist Paul M. Romer. The technological seeds planted in the early '90s need cheap and plentiful capital to flower. A quarter-century of slow growth has robbed America of some of its spirit. The old metaphor of the American economy—a rapidly expanding pie from which everyone can take a larger and larger slice—has been replaced by the notion of the zero-sum game, where each winner's gain is some other player's loss.

To restore the old spirit, Americans must go back to economic basics. Consume less now. Put more away for the future. Invest wisely. Regardless of what political candidate may promise, there is no surer way to guarantee a bright tomorrow for the U.S. economy.

By Mike McNamee, with Paul Magnusson, in Washington

Investment in physical capital alone won't ensure fast growth: The U.S. needs better educated workers, too



DECISIONS ARE TOUGHER.
TIME IS CRITICAL.
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'IT'S PUT UP OR SHUT UP TIME'

Nabisco's CEO scrambles to stop the snackmaker's slide

After H. John Greeniaus became chief executive of Nabisco Inc., one of his standard management tactics was to pass out report cards to subordinates. At quarterly meetings, he assigned division heads grades ranging from A to F, based on meeting performance targets.

Now, 17 months since parent RJR Nabisco Holdings Corp. sold off 20% of its Nabisco unit to the public, it's Greeniaus' turn to worry about his marks. As runaway costs, price wars, and slowing sales of once-hot SnackWell's cookies eat away at earnings, performance at the \$8.3 billion Nabisco has left some investors with a bad taste. With the stock at 33%, shareholder returns since the January, 1995, IPO tally just 36%, well behind the 49% gain of Standard & Poor's 500-stock index for the same period.

So Greeniaus, 51, is cleaning house at the Parsippany (N.J.)-based company he has headed since 1987. On June 24, he announced a major restructuring. Nabisco will cut 4,200 jobs, streamline production, and ax underperforming products. The company will also take a \$428 million pre-tax charge to second quarter earnings. Concedes Greeniaus, a 19-year Nabisco marketing veteran who made headlines by siding with Henry R. Kravis in the 1989 battle for RJR Nabisco: "Our performance is not up to the standards that we traditionally have met."

That's putting it mildly. The IPO came to market amid rosy projections. Fueled by the



LOW-FAT FOCUS: Greeniaus bet on line extensions

smash hit of the SnackWell's line of fat-free cookies, 1994 operating income (before amortization) soared 17.2% in 1994, on revenues up 9.5%. Wall Street expected more of the same. But in 1995, income rose just 1.5%, to \$1.1 billion, on sales up 8%. "Here is a management team that looks good in presentations," says Robert Sanborn, portfolio manager at Harris Associates LP, which holds 2.2 million shares. "It's put up or shut up time."

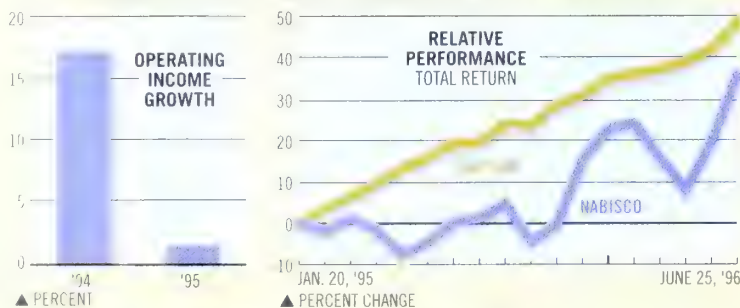
Greeniaus places some of the blame on price wars in Nabisco's two largest markets, cookies/crackers and nuts. Rivals Keebler Co. and Fisher Nut Co. went on the block last year, and both lowered prices to boost sales, says Goldman, Sachs & Co. analyst Nomi Ghez. Worse, the battle began just as a capital-spending plan peaked. "It was sheer bad timing," Greeniaus says. The two units saw their share of estimated operating profits fall from around 60% in 1994, to roughly 50% last year.

The price wars are over, but Nabisco's problems aren't. Sales of SnackWell's also show signs of weakness. Competitors such as Keebler copied the low-fat format just as Nabisco cut back on SnackWell's promotions. And analysts say consumers realized that fat-free isn't calorie-free. For the year ended Apr. 21, unit sales of SnackWell's cookies dropped 11%, according to Chicago-based market researcher Information Resources Inc. "The whole category is down," says Michael Rourke, senior vice-president of marketing and corporate affairs at Great Atlantic & Pacific Tea Company Inc. a customer. "There are so many other products people are picking up."

That's a troubling trend for Nabisco, which has bet so heavily on SnackWell line extensions that some observers worry about brand dilution. "They put SnackWell's stamp on anything that stands still long enough," says Al Ries, marketing consultant at Ries & Ries in Great Neck, N.Y. Yet the name alone is no guarantee: While SnackWell's new breakfast bars could hit \$300 million in sales this year, pretzel and chips never got off the ground. To reverse crumbling cookie sales, Greeniaus is counting on a new low-cal version delayed by taste problems but due out by mid-1997. And he argues there's plenty of growth left. "I don't believe we have come close to taking SnackWell's too far," he says.

At the same time Nabisco has scramble

NABISCO'S LESS-THAN-TASTY RETURNS



DATA: COMPANY REPORTS, BLOOMBERG FINANCIAL MARKETS

or non-SnackWell's successes. Last year, Nabisco introduced 77 new products, including low-fat Planters nuts and non-it Newtons Cobblers. Now, Greeniaus admits Nabisco may have spread itself too thin. "We probably overdid our new-product activity by about 20%," he says. Anything that looked half decent, we're in with." As part of the restructuring, Nabisco will sell off some brands and trim slow-selling items.

SPECIAL DELIVERY. High costs have been another sticking point. Greeniaus blames "sloppy management" for allowing fixed costs to get out of hand, impacting on the success of SnackWell's. Nabisco poured \$1.36 billion into modernizing plants and expanding capacity over the past three years. But the build-up came onstream just as SnackWell's began to slip. Nabisco has also paid a price for its costly distribution system: Its biscuit unit uses its own trucks and salespeople to deliver directly to retailers' shelves, unlike many rivals. The system offers better customer relations and closer control over what goes into the stores, and Greeniaus has left it in place for now. But distribution could come under greater scrutiny if the restructuring doesn't yield results.

Greeniaus, known as an aggressive, hard-driving manager, is wasting no time shaking up the executive suite. Last December, he named former international chief James J. Postl, known as a cost-cutter, to run the key Biscuit div. Outsiders have been brought in as chief financial officer and head of international, and buyouts have cut middle-management ranks. "Greeniaus doesn't suffer mediocrity well," says Gary M. Libel, a principal of New England Consulting Group. "Those that cannot take it won't be there a year from now."

The question is whether Greeniaus' restructuring will make the grade. Investors welcomed the moves but are cautious. "It remains to be seen if the culture has been changed to be more cost-conscious," says Gregory L. Jackson, portfolio manager at Nabisco shareholder Yacktman Asset Management Co. Greeniaus—who also became chairman in May—denies that the changes are linked to Wall Street pressures for a spin-off. Still, investor Carl C. Icahn continues to push for one, and RJR's board could decide to spin off its remaining 80% stake as early as 1997. So reassurance to improve won't go away. "We want any buyer to understand what a well it is," says Nell Minow of the Pens Fund, an RJR shareholder. "We don't want a fire sale." With a final report card not too far off, Greeniaus has lots of homework to do.

By Lori Bongiorno in New York

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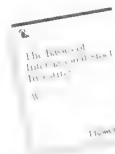
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A STAR IS REBORN

Investors hustle to land parts in Times Square's transformation

Before Hollywood, there was Times Square, world famous as the nexus of American popular culture in its first Golden Age. Well into the 1930s, New York's Times Square flourished as the national center stage for plays, movies, and pop music. By the 1940s, it had settled into a gradual decline that accelerated in the 1960s as pornography and street crime took root. Sporadic attempts at cleaning up the district went nowhere. In 1992, officials scuttled an ambitious plan to redevelop 42nd Street, the epicenter of the district's blight. Times Square seemed more hopeless than ever, a symbol not only of the sleazy side of big-city America but also of the intractability of its decay.

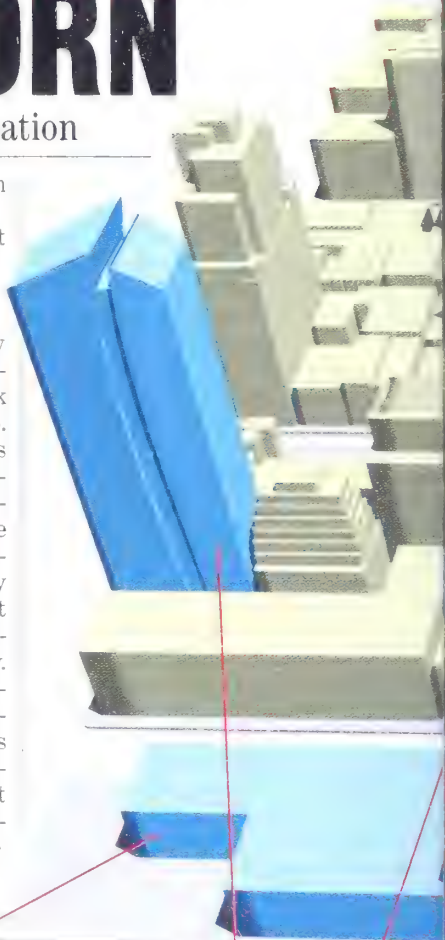
Even so, today Times Square is on the verge of rebirth as a shiny new centerpiece of the Entertainment Economy and as one of New York's major retail centers. Some of the world's largest media and entertainment companies—Bertelsmann, Disney, Condé Nast—have made a commitment to Times Square, and many others are poking around, as are legions of brand-name retailers. Although the look of 42nd Street won't change radically for another two years, the investment infrastructure of the new Times Square is now in place. The bets are down—and they are huge: at least \$4 billion. "It's like a snowball coming down the hill," says Andrew Tansley, executive director of Tussauds Group Ltd. "Now, the question is not, 'Is it going to happen?' but rather, 'Can you keep up as it happens?' Things are really motoring."

"THE DEUCE." At 42nd Street and Eighth Avenue, Tishman Realty & Construction Co. is pressing ahead with its first New York development in years—a \$300 million hotel and entertainment-and-retail arcade. A bit farther east along "the Deuce," as this stretch of 42nd was known at the height of its infamy, Forest City Ratner Cos. is readying a \$200 million complex to feature a Madame Tussaud's wax museum and an

AMC Entertainment Inc. multiplex with at least 25 screens.

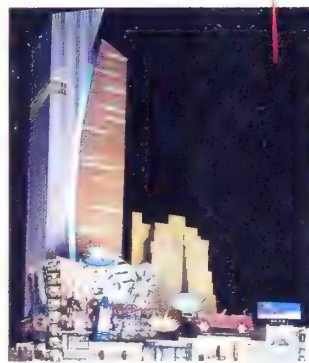
In July, one of Manhattan's richest real estate families, the Dursts, plans to begin clearing a huge site at Broadway between 42nd Street and 43rd Street for what will be the first new skyscraper groundbreaking in Manhattan in nearly a decade. And a half-block away, on 42nd Street, Walt Disney Co. has reached the halfway mark in its painstaking renovation of the New Amsterdam Theater, a Beaux Arts masterpiece that opened in 1903 and was the grandest of all the Times Square theaters. The Disney, Durst, Forest City Ratner, and Tishman ventures are just the most significant of a dozen development projects that are now under way.

Whether measured by acreage condemned, dollars invested, or sheer complexity, the 42nd Street makeover ranks as perhaps the most ambitious inner-city reclamation ever. Yet the direct government investment has been a pittance—\$64 million. Along the way, the strategy was altered so radically that the project's biggest backer was left



FOREST CITY RATNER

It has put up \$200 million for a Madame Tussaud's wax museum, a 25-screen multiplex, and shops



TISHMAN

For \$300 million, it will wind up with a hotel and an entertainment arcade

DISNEY

Its agree to revamp the New Amsterdam Theater. Beaux Arts gem. was waving a magic wand. Investors piled in

■ Proposed ■ Existing

MORGAN STANLEY

Wall Street came to 47th Street when the brokerage set up its main office amid the honky-tonk

2 TIMES SQUARE

Renovated a few years ago, it is the Square's most renowned billboard

BERTELSMANN

The German media colossus occupies two-thirds of its \$350 million property

1 TIMES SQUARE

This landmark tower has been acquired at auction for \$27.5 million

42ND STREET

7TH AVENUE

BROADWAY

CONDE NAST

The owner of *Vanity Fair*, *Vogue*, and *Glamour* bestowed cachet on 42nd Street by leasing one-third of the planned Durst tower for its editorial offices

out in the cold, with little to show for a \$300 million investment, while the developer who was its most obstinate foe was transformed into its champion. And it might all have gone for naught but for a puny \$8 million investment by Disney, whose name is as synonymous with wholesome family fare as Times Square is with X-rated attractions.

Government officials across the country are finding inspiration in Times Square's comeback, for many older cities are hoping to revive depressed commercial districts by reinventing them as entertainment centers. But in the view of many of its central players, the revival of Times Square is a singular achievement—and nobody's prototype. "Times Square is Times Square, and even New York only has one," says Brendan Sexton, president of the Municipal Art Society of New

York. "But there is the lesson that urban renewal solutions must be informed by what is distinctive about a place."

Times Square's revival is the product of two concentrated bursts of redevelopment activity, the second of which is now under way along 42nd Street. The first, triggered by new zoning rules enacted in 1982, put a dozen new office buildings and hotels on the drawing board in upper Times Square, from 45th to 50th Streets. Convinced that rezoning alone would not suffice for the Deuce, officials devised a plan to condemn 13 acres and lard them with tax incentives to attract private developers. The linchpin of the 42nd Street Development Project was a complex of four colossal office towers to be developed by Times Square Center Associates (TSCA), a partnership of Park Tower Realty and Prudential Insurance Co. The TSCA agreed to cover most of the costs of condemnation and of renovating a subway station and six theaters.

BEYOND HOPE. The combined effect of the 42nd Street plan and all the zoning-induced construction would have been to bulldoze the old Times Square and replace it with an office-tower canyon in the mold of neighboring Sixth Avenue. This was logical to the extent that it offered private capital the highest returns with the least possible risk. But it was also predicated on the notion that Times Square had deteriorated beyond hope of redemption by less drastic means. "Times Square is a cancer, a blot on the city," Park Tower's principal owner, George Klein, said in 1984. "We're going to clean it up."

Appalled by the sterility of the plan, which also included a giant merchandise mart and hotel, a dozen civic groups joined forces with Broadway theater interests and the Municipal Art Society to champion the continuation of Times Square as a low-rise, high-wattage entertainment district. Unlike the typical preservationist cause, this one developed a broad commercial following, for its arguments were ground-

ed as much in economics as aesthetics. Even at its most decrepit, Times Square remained an offbeat venue of legitimate commerce, where tourists by the millions came to gawk at advertising.

There was no hope of halting the wrecking ball in boomtown Manhattan, but the city again amended the zoning code "to ensure that the unique and valuable sense of place of Times Square will be retained." The most novel of the new rules mandated that facades must be fitted with outsize illuminated signs. The notion of having to bedeck their marble-and-granite palaces with neon outraged developers, none more so than Klein.

In lower Times Square, the sign issue was rendered moot as the 42nd Street project was stalled by 47 lawsuits challenging its every aspect. The litigants included the Durst family, which had hoped to erect an office tower on part of the site the state had awarded to the TSCA. The Dursts pressed on, even taking a long-term lease on the six theaters included in the government plan. "We hoped to show that the theaters could be redeveloped without subsidy," says Douglas D. Durst, the third-generation president of the Durst Organization.

By the time the new office towers in upper Times Square were completed in 1990, the Manhattan real estate market was in the early throes of a deep contraction. Unable to attract tenants even at sharply discounted rents, the developers of three just-completed office towers strung along Broadway from 45th Street to 49th Street put their handsome, empty skyscrapers into bankruptcy.

DELAYS, DELAYS. Meanwhile, down on 42nd Street, the moment of truth had arrived for the TSCA. By now, all the legal challenges had been resolved in the government's favor, and the next step was for Prudential to post a \$241 million letter of credit that the state would use to pay for 9 of the 13 acres targeted for condemnation. The devel-

opers had yet to sign up a single tenant, and the prospect of filling 4 million square feet in a weakening market was daunting, but Prudential put the money down as promised. "I couldn't believe it," Durst says. "I never thought they'd take such a big risk."

By 1992, Prudential was sorry it had. The TSCA still hadn't found an anchor tenant and had no likely prospects. With the real estate market worse than ever,

now would be refurbished as restaurants, stores, and state-of-the-art amusement venues, all done up in bright light and outré displays. In addition, the state would condemn the last remaining stretch of pornographic blight along 42nd, extending the renewal zone all the way to Eighth Avenue.

GETTING ANIMATED. City and state officials began soliciting entertainment purveyors of all sorts. "At one point, we

were kind of enthralled with mud wrestling," says Robertson. The first major company to seriously consider 42nd Street was Tussaud Group, a division of London's Pearson PLC. Tansley, Tussauds' executive director, flew in on several cautious scouting expeditions. "We were interested," he says. "But we didn't want to be the only ones."

Enter Walt Disney Co., which over the years had repeatedly declined invitations to invest in Times Square. In late 1992, Disney decided to make a stage show of its animated feature *Beauty and the Beast* and was scouting Broadway real estate. In March, 1993, Disney Chairman Michael D. Eisner made a spur-of-the-moment inspection of the New Amsterdam Theater. The place was



BROADWAY BABY

Durst's 48-story building will be Manhattan's first groundbreaking for a skyscraper in 10 years

the developer and the government jointly decided to delay construction indefinitely. By this time, the plans for the merchandise mart and hotel also had come to naught, sticking the state with 1.5

million square feet of dilapidated, mostly vacant properties. Disaster loomed. "We had become a pariah politically," admits Rebecca Robertson, the head of the government agency created to redevelop 42nd Street.

Robertson and her remaining allies decided to shift emphasis from office-tower development to rehabilitating 42nd Street as an entertainment hub for the masses. The TSCA resisted the change in direction at first but fell into line when the new interim plan—42nd Street Now!—was unveiled to a public acclaim unknown to the old approach. Buildings that were to have been razed

ruin, but Eisner was intrigued by its possibilities. And Robertson was determined to land Disney at all costs. "We were more than prepared not to fool around," she says.

By January, 1994, Eisner and the government had reached a tentative agreement on terms highly favorable to the company. Disney would invest \$5 million, and the state and city together would lend the company \$26 million and 3% to cover the balance of the cost of remodeling the New Amsterdam and adding 200 seats. Disney set two conditions to a final deal: Robertson would have to sign at least two more major entertainment companies for 42nd Street, and officials would have to make good on their promises and cough up the \$35 million needed to buy out the remaining X-rated shops.

The world reacted as if the company had touched 42nd Street with a magic wand. "Before Disney, most of the call

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A TIME-HONORED TRADITION IN MONEY MANAGEMENT

I got were from Times Square property owners trying to get me to calm the fears of prospective tenants about coming to Times Square," says Gretchen Dykstra, the director of the Times Square Business Improvement District. "After, it was all brokers trying to get a piece of the action."

AMC soon took an option on a site that included two historic theaters. Tishman Construction was selected as the developer of a hotel-entertainment complex at the newly condemned Eighth Avenue end of the Deuce. Tussauds Group worked up a plan to acquire the landmark tower 1 Times Square Plaza but was outbid at auction. Forest City Ratner then negotiated its own deal with the state to develop a large complex to house AMC, Tussauds, and other tenants. In July, 1995, Disney committed fully to restoring the New Amsterdam, which will reopen next spring as a venue for Disney's own productions.

Meanwhile, the TSCA invested an additional \$25 million to refurbish the dozen low-rise buildings that stood on its Seventh Avenue site for retail use and to build a Disney

WE'RE IN THE MONEY

Virgin's shop in the Bertelsmann building pulls in \$1 million a week—twice its target

Store, which will be hooked into the New Amsterdam. "We leased all of it faster than expected and at very attractive rents," says Brian Murphy, managing vice-president at Prudential Realty Group. "Forty-second Street is going to be a fantastic address."

GLITZ AND GLAMOUR. For Prudential, though, the real question was whether it would become a corporate address. If the insurer was ever to see a return on the \$300 million it had sunk into 42nd Street, it would eventually have to put up a couple of office towers. By 1995, the Manhattan office market was showing signs of life, but with Prudential in the midst of reevaluating its plans for commercial real estate, the insurer was in no hurry to build in Times Square or anywhere else.

Sensing Prudential's enervation, Durst decided to try to buy his way into the project that his lawsuits had failed to stop. If Durst could combine the large

parcel he had assembled with the dormant TSCA tract adjacent to it, he would have an ideal site for a new office tower. Through an intermediary, Durst gingerly approached Klein, who agreed to meet with his old nemesis. "The mood," says Durst, "was somber." Although Klein wanted to hang on to his dream site in its entirety, Prudential was willing to deal. The Durst-Prudential negotiations were arduous and broke off entirely several times. In the end, Durst agreed to pay about \$75 million for about one-fourth of TSCA's acreage, and Klein reluctantly went along.

In May, Condé Nast Publications Inc., publisher of *Vanity Fair*, *Vogue*, and a dozen other glossy magazines, agreed to lease about one-third of Durst's

recognizable. In many ways, though, the entire Times Square district has already been reborn. There are now more legitimate theaters—36 at last count—than X-rated ones. Only 20 porn palaces remain, down from 50 two years ago, and the incidence of serious crime has fallen 55% since 1993, exceeding the average rate of decline for Manhattan. Safer, cleaner streets have spurred ticket sales on Broadway, which, during the recently completed 1995-96 season drew the largest audiences in 15 years. Literally as well as figuratively, the Great White Way is aglow, for Times Square's famous signs again are as numerous and luminous as in their 1950s heyday.

All three of the office towers that stood empty and bankrupt four years



planned 48-story tower, to be named The Condé Nast Building. The \$500 million project has already conferred a provisional cachet on 42nd Street as a corporate address, for Condé Nast is one of the city's most glamorous tenants and the Dursts are known as cautious developers who have made few missteps over the years.

Although Tishman Construction won't begin demolition on its site for six months, it has already found tenants for 70% of the 200,000 square feet of space in its arcade. It is so confident of leasing the rest at even higher rents that it is holding it off the market. Meanwhile, Forest City Ratner has lined up tenants for all but 40,000 of its 400,000-square-foot development. "There won't be room for all the retailers who will want space on the new 42nd Street," predicts John L. Tishman, the Tishman organization's chairman.

In two years, 42nd Street will be un-

ago have been purchased, at what have proved to be bargain prices, by top-flight companies for use as headquarters. Morgan Stanley & Co. snapped up both 1585 Broadway and 750 Seventh Avenue, while Bertelsmann bought 154 Broadway. The German media colossus occupies two-thirds of the building and has leased out the rest to tenants that include Sony Theaters and Virgin Retail Group. Virgin recently opened an elaborate entertainment superstore that is pulling in \$1 million a week—double its expectations.

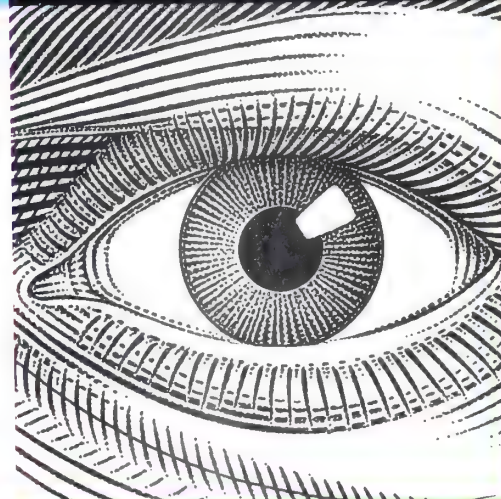
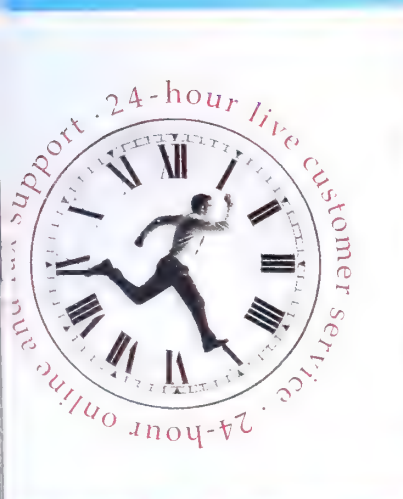
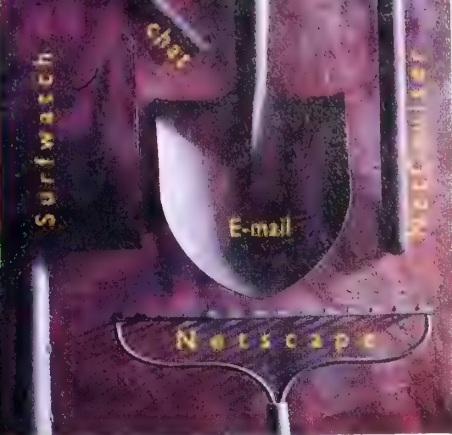
In the Cyber Age, no place—not even Hollywood—will ever again dominate popular culture the way that the old Times Square did. But if all goes according to plan, by the turn of the century, Times Square—the self-styled "Crossroads of the World"—will have reestablished itself as a live entertainment center nonpareil.

By Anthony Bianco in New York

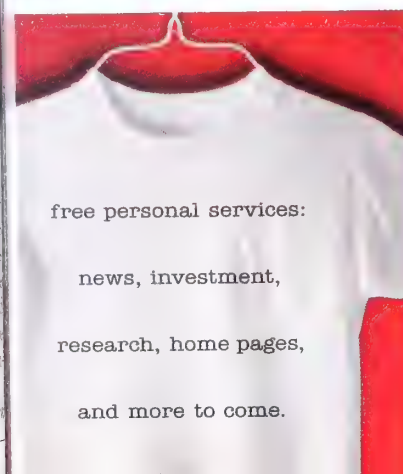
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STOCK AND BOND RISK: FORGET WHAT YOU KNOW

New investment patterns and Fed practices have changed the game

In the wake of 1995's rip-roaring stock market gains and the neat follow-up in 1996, many investors are worrying about whether to take some money off the table. From their newspaper in the morning to the television at night, they are bombarded with talk about the market's riskiness. The solution to such angst, they are told, is simple: Lower the risk level in your portfolio, and sleep better at night by moving some money out of stocks and into the sedate world of fixed-income investments.

Investors who are seduced by such advice may be in for a rude shock. Sure, big swings in the stock market within the trading day make it seem riskier lately. But dig deeper, and a different picture emerges. According to Chicago-based Ibbotson Associates Inc., the Standard & Poor's 500-stock index actually was less volatile in the past five years than in the previous five. At the same time, the market's returns were greater (chart). So investors got fatter returns with less risk, not more.

Many investment strategists say the bond market is the big swinger these days—and hardly a safe haven. Its reputation for stability is a hangover from a very different bond market of decades ago. While its volatility has come down in recent years, it is riskier than many investors may realize.

To gauge the risk of an investment, statisticians rely on a measure called the standard deviation. After calculating the average return of an investment over a given period, statisticians measure how much returns have deviated from the average. The greater the fluctuation, or standard deviation, the greater the chance of wide swings in returns, both above and below the average—and the greater the risk.

An analysis of the standard deviation of the S&P 500 deflates the idea that today's stock market is extremely volatile. In fact, the period from 1991 to 1995 was the least volatile five-year period for the index since its inception in the 1920s. From 1991 to 1995, the S&P 500 deviated just 11.7% from its average, or mean, return. That compares with a far-greater 21.5% from 1986 to 1990.

A DIFFERENT DOW. Ibbotson looked at monthly numbers, but daily numbers also show a less volatile stock market. Jeremy J. Siegel, a finance professor at the Wharton School of the University of Pennsylvania and author of *Stocks for the Long Run*, notes that the average day-to-day price change in the Dow, at less than 0.65% today, is slightly below the long-term average of 0.69%.

Still, the popular perception is that the stock market is highly volatile. One oft-quoted statistic seeming to support

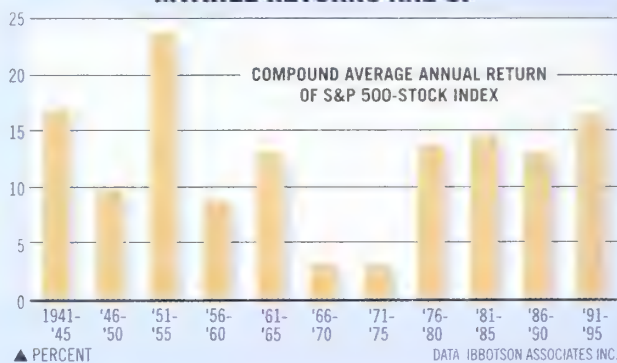
that notion is that the New York Stock Exchange's 50-point "collar," which limits certain kinds of trading when the Dow moves 50 points, has been triggered a record 58 times in 1996. But couching market volatility in points, rather than in percentages, makes market fluctuations appear far worse than they are, says Abby Joseph Cohen, co-chair of the Investment Policy Committee at Goldman, Sachs & Co. In 1990, when the NYSE's collar was introduced, a 50-point move represented about 2.5% of the Dow. Today, a 50-point move is less than 1% of the Dow.

Investors have themselves to thank for the stock market's reduced risk. The huge inflows into equity mutual funds have dampened the market's moves. Not only have investors shifted money out of bonds and savings deposits and into stocks; they have also directed more of the money in the growing universe of tax-deferred retirement

STOCK VOLATILITY IS DOWN...



...WHILE RETURNS ARE UP





period, mainly because of high inflation. Investors have been whipsawed by the bond market's wild swings. In 1994, the market had its worst year ever. In 1995, it had one of its best years. And in 1996, the rise in long-bond yields from 5.95% to 7.04% means that the 30-year bond is on track to have another big year on the downside, measured by total return, says James A. Bianco, director of research for Arbor Trading Group Inc. in Barrington, Ill.

The fickleness of bond investors has added to that market's volatility. Until a few years ago, the flows into mutual funds were almost evenly split between stock and bond funds. But after 1994, when the 30-year Treasury lost 11%, bond funds had outflows of \$43.4 billion. Some bond funds holding 30-year Treasuries lost more than 17% of their value.

Painful memories of 1994 kept many domestic investors out of the bond market in 1995. That year, buoyed by funds from foreign investors, the bond market had its third-best year ever, with the 30-year Treasury up 34.1% as the Federal Reserve eased rates. But since the stock market did even better, with a 37.5% return, investors continued to pull money from bond funds, albeit just \$4.1 billion. So far in 1996, bond funds have

they matured. Fixed-income securities are more actively managed today, so prices bounce around more, says Morris W. Offit, chairman of Offitbank, which specializes in fixed-income management. "You can take a fixed-income instrument today and by leveraging it through derivatives, create an instrument that has a risk profile well beyond the most unseasoned common stock," says Offit.

WILD RIDE. The yield on the long bond has been all over the map in the past few years. It moved from a 22-month low of 5.77% in October, 1993, to 8.16% a little more than a year later. It then fell below 6% last December and now sports a yield of about 7.04%. Inflation, meanwhile, has stayed in a narrow band of 2.5% to 3%.

Jeremy Siegel places much of the blame for the long bond's volatility on Fed policy. He argues that the Fed isn't adjusting short-term rates frequently enough. He takes issue with the Fed's practice of announcing moves in short-term interest rates in conjunction with Federal Open Market Committee meetings, which take place eight times a year. "When the Fed doesn't allow the short-term interest rate to fluctuate in response to market forces, the entire burden of adjustment falls on the long-term rate, leading to wide swings in the market," says Siegel.

The presence of more speculative players in the bond market is also ramping up risk. At a time when the bond market is not getting much in-

In the past few years, huge inflows from investors have contributed to the reduced risk in stocks. But outflows from the bond market have helped to increase the turbulence there

vings plans, such as 1(k)s, into stocks. Since that money is deducted regularly from payroll checks, it gives the market a steady stream of funds. Investors have also helped the market by treating market dips as buying opportunities, which has kept the stock market's drops small.

It's a different story in the bond market. Standard-deviation statistics tell the tale. Despite low inflation, the volatility of an investment in the long-term Treasury bond was 8.9% from 1991 to 1995. That's below the 12.6% standard deviation in the previous five years. But look further back, and that 8.9% looks pretty high. In the mid-1960s, with inflation at about the same rate as today, the standard deviation was only 2.5%. In fact, in the 14 five-year periods from 1926 to 1995, only four periods displayed higher volatility than the 1991-95

seen inflows of \$9 billion. That compares with flows of more than \$121 billion into stock funds.

There are more fundamental reasons for the increased risks of the bond market. The deregulation of the banking and the financial industries in the 1970s and 1980s injected a lot more volatility into interest rates and bond prices. "Before then, interest rates had been pretty much fixed by the government," says Robert Commisford, a senior consultant with Ibbotson. Now, with so many more players in the market, both in the U.S. and abroad, bond prices can gyrate with lightning speed.

The nature of fixed-income investing has also changed. Gone are the days when investors simply held bonds until

vestor money to act as a shock absorber, the rapid-fire buying and selling of hedge funds is magnified. A recent hedge-fund strategy that unsettled the bond market involved borrowing in yen to buy Treasuries. "Since the summer of 1995, when the hedge fund's yen/Treasury bond arbitrage trades started coming in, the bond market has become the domain of the big arbitrageur," says Mitchell J. Held, chief economist for Smith Barney Inc.

Lower volatility in the stock market doesn't mean that investors won't have a bumpy ride. But those opting for the "safety" of bonds should be aware that they may be setting themselves up for some sleepless nights.

By Suzanne Woolley in New York



INVESTMENT BANKING

THE BRAIN DRAIN AT ING BARINGS

Since the merger, its equities team has been damaged

Fifteen months ago, Hessel Lindenberg got a hero's welcome from employees of Barings PLC. In early March of 1995, the now chairman of ING Barings strode into Barings' London trading floor to announce that the Dutch insurance and banking giant had won approval to buy Barings for \$1.02 billion. That meant Britain's oldest merchant bank, which had gone bust a few weeks earlier after huge losses rung up by Singapore trader Nicholas Leeson, would be saved from near-certain breakup. With enormous relief, hundreds of Barings stockbrokers and analysts gave Lindenberg a standing ovation.

But neither Lindenberg nor Aad G. Jacobs, chairman of ING Group, is getting much applause these days. A more noticeable sound at ING Barings is the swoosh of the revolving door. In the last month, Deutsche Morgan Grenfell poached at least 60 members of Barings' top-rated but money-losing Latin American equities team, leaving in places skeleton crews. ING Barings' Americas unit chairman, Lane Grijns, is now searching for an experienced equities hand to be-

come his president, after having two ING people go through the job since last November. ING Barings' well-respected global equities strategist in London, Michael Howell, is starting his own consulting firm, taking the global head of equity sales and three others. A few members of the Asian equity team, including former Asian equities head Andrew Fraser, have already left, and larger numbers may be set to bolt, too.

Lindenberg calls the defections so far "everyday" occurrences, and Grijns

WHY THE ING-BARINGS ALLIANCE HAS HIT A SNAG

- Numerous defections from ING Barings' key equity group, mainly among research specialists in Latin America
- Clash between Barings' high-flying equity culture and ING's more sedate commercial-banking and insurance culture
- Serious turf battles between ING's debt operations and Barings' equity group in ING Barings' Latin American business
- Lack of experience by ING executives in equities trading, stockbroking, and research

DATA BUSINESS WEEK

BEATSON-HIRD: *At least 60 people left Barings with him when he was fired*

says they're "not a disaster." It's true that escalating salaries in global banking are prompting a frenzy of job-hopping everywhere. But ING's staff losses also suggest that its high-profile acquisition of Barings, which just a few months ago seemed to be a big success, may be having problems. By most accounts the asset-management and corporate-finance businesses of the old Barings are doing fine. But the equities unit is struggling. Since research and stockbroking are crucial to cementing relationship with corporate clients, the risk is that the equity side's troubles could sidetrack ING's ambitions to build a global investment-banking leader in the emerging markets.

ING intends, among other steps, to rebuild its key Latin American equity operation. But new hires won't solve the management problem that's contributed to the gutting of one of the industry's top equity crews. "You don't get a team to move unless there's a serious malaise," argues Richard Watkins, CEO of LatInvest Securities in London. Indeed, former high-level Barings executives say the equities unit is suffering from tangled reporting lines, a low priority placed on research and stockbroking by the Dutch parent, and a clash between Barings' high-flying equities culture and ING's commercial-banking and insurance roots.

TURF BATTLES. Nowhere has that been clearer than in Latin America, where Barings had built up a formidable presence. Jonathan Beatson-Hird, 36, the former managing director of Latin American equities, says his group "suffered hugely from structural and cost problems" associated with integrating ING and Barings' businesses. His team, he says, was hobbled by frequent turf battles and confused reporting lines.

In April, Beatson-Hird began talking seriously about joining Deutsche Morgan Grenfell. When ING Barings learned of this, Beatson-Hird was fired, says Lindenberg. Within weeks many of Beatson-Hird's colleagues followed him. ING insists that just 60 or so people left—not 73 as Beatson-Hird claims—after DMG offered to boost their salaries by up to 100% and guarantee bigger bonuses for two years. But the lure of fatter pay checks was not the only draw. "Morale was horrible," explains



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CUSHMAN & WAKEFIELD WORLDWIDE

Mexico staffer who joined the exodus.

"It was a blow, but it's not something we won't recover from," says Walter "Rocky" C. Butler, general director of the ING Barings Mexican operations. "By and large, investors are being patient," he says. Although ING plans to begin hiring soon, it may only replace half the Latin America people who left. And Grijns says it will not pay the inflated prices Deutsche has been shelling out to lure away Barings' people. To stem further defections, ING two weeks ago set up a new global pay plan with stock options and higher bonuses.

The threat of a further talent drain raises a troubling question: What did ING get for the guilders it spent on Bar-



JACOBS AND LINDENBERGH: *ING hopes a new pay plan will stop defections*

ings? To be sure, it nabbed some strong businesses. Baring Brothers, the group's investment banking arm, vaulted to the top of the Europe league's M&A tables last year, completing deals worth nearly \$35 billion. As well, Barings has helped transform ING into a major asset manager, more than doubling its external funds under management to \$65 billion. **"GREAT KNOCK."** But the trouble spot remains equities. In part due to slow trading in emerging markets for much of last year, ING has been forced to inject nearly \$300 million to meet capital requirements. Lindenberg says there could be further recapitalizations ahead.

Clearly, the high-profile defections and the mounting signs of unrest aren't what this quiet Dutch insurer bargained on when it bid for Barings. "They've taken a bloody great knock," says Alexander T. Murray, a Barings Securities founder who left the firm in March. "But don't underestimate ING. It's got the financial resources and the will to make this work." That may be, but it's likely to be some time before Lindenberg or ING hear any applause from the Barings trading floor.

By Julia Flynn in London, with Alison Rea in New York, Elisabeth Malkin in Mexico City, and Ian Katz in São Paulo

MUTUAL FUNDS

WHY MORGAN STANLEY BOUGHT A CASE OF THE BLAHS

Van Kampen's distribution network could be worth it

What's a top-drawer investment bank doing buying a decidedly second-tier mutual-fund firm? That's a question many people in the fund business are asking about Morgan Stanley Group Inc.'s June 24 agreement to purchase Van Kampen/American Capital Inc. for \$1.1 billion. Morgan Stanley has a ready answer: "We see an opportunity to build on a solid investment performance record and make that a top-notch record across all asset categories," says Philip N. Duff, Morgan Stanley's chief financial officer. The McGraw-Hill Companies, publisher of *BUSINESS WEEK*, also bid for Van Kampen.

Yet, with \$57 billion in mainly mutual-fund assets under management, Van Kampen has an undistinguished record when it comes to its stock and bond funds. "Van Kampen/American Capital is not a stellar performer," says Jim Raker, an analyst at Morningstar Inc. "Morgan Stanley's challenge is to turn mediocre funds into good funds." Adds Dennis Dolego, a partner at Financial Research Corp., a Chicago mutual-fund research firm: "It remains to be seen whether Morgan Stanley can compete with AIM, Fidelity Advisor, Putnam, American, and the Franklin funds."

RAPID CONSOLIDATION. Franklin, which already owns Templeton Funds, is set to become an even tougher competitor. On June 25, in another move that reflects the rapid consolidation of the mutual-fund business, Franklin agreed to buy Heine Securities Corp., parent of Michael F. Price's Mutual Series Funds. Franklin will pay \$610 million for \$17 billion in four equity funds. Price says Franklin gives his firm and his shareholders a boost. "If Franklin was good enough for John Templeton, it's good enough for me," says Price. All of his funds earned five stars, Morningstar's highest accolade.

Van Kampen, in contrast, has only one five-star fund. And only one of its five largest equity funds rates better than average (table). Of the five largest bond funds, just one merits a better-than-average rating. Redemptions exceed new investments in a number of its funds, according to Financial Research Corp. Two of Van Kampen's flagship eq-

uity funds, Pace and Comstock, have seen \$10 million to \$25 million per quarter in cash outflows for the past few quarters at a time when equity fund sales industrywide have been booming.

Morgan Stanley believes it can beef up Van Kampen's performance with its own top-notch money-management team headed by investment guru Barton M. Biggs. Most important, Van Kampen gives Morgan entrée to the individual investor. "We are marrying our retail distribution and service skills with Morgan Stanley's product capability," says Don G. Powell, Van Kampen's CEO. "Together we will be a stronger firm than apart." Van Kampen has agreements with 2,500 organizations, including brokers and banks, which assures Morgan Stanley shelf space for new funds as even for insurance products it wants to create. And Van Kampen has consistently won awards for its customer service.

Service is important, but what sets mutual funds is performance. Mike Pri has it. To make Van Kampen pay off Morgan Stanley's got to get it.

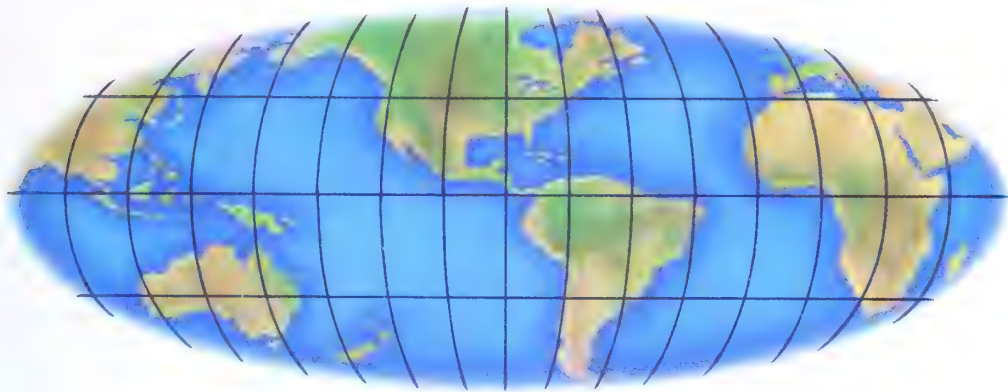
By Leah Nathans Spiro, with Jeffrey M. Laderman in New York

Van Kampen's Record: Just Average

FIVE LARGEST EQUITY FUNDS	MORNINGSTAR RATING
PACE A	★★★
EMERGING GROWTH A	★★★★★
COMSTOCK A	★★★★
ENTERPRISE A	★★★★
EQUITY-INCOME B	★★★★
FIVE-LARGEST BOND FUNDS	MORNINGSTAR RATING
U.S. GOVT. A	★★★★
GOVT. SECURITIES A	★★★
INSURED TAX-FREE A	★★★
MUNICIPAL INCOME A	★★★★
TAX-FREE HIGH YIELD A	★★★★★

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DATA: MORNINGSTAR INC.



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NOW THE MEDIUM IS THE MESSAGE BOARD

Diana's wild ride shows how cyberpostings move stocks

The stock symbol for Diana Corp. is DNA—the same as the building blocks of life itself. But lately, Diana stock has been death incarnate. In just four weeks, this Milwaukee-based company's stock has fallen from 103 on May 28 to 39½ on June 26—after climbing all the way up from 5 a year ago. Some of the gyrations were caused by ordinary market influences. But for much of Diana's wild ride, the stock was sent careening by a potent new force in the markets: the power of online services.

Diana's rise was fueled by postings

“There is a rumor that MCI might be interested in DNA—or something like that.”

VALUESPEC

*On a Motley Fool message board,
Mar. 21, 1996*

online—particularly America Online Inc.'s Motley Fool electronic bulletin boards. But so was its fall—and in a manner so troubling that it has apparently drawn the interest of regulators. The New York Stock Exchange, where Diana's stock is listed, is investigating trading in the stock, according to company officials. Diana executives maintain that the company's shares were driven down by disclosure of inside information that was posted on Motley Fool message boards. If so, the implications could be serious for the online world, which is getting increased scrutiny from regulators as a medium for market manipulation. Editors of the Motley Fool, whose stock recommendations have been hammered in recent weeks, did not return phone calls seeking comment.

In Diana's case, the negative information posted on Motley Fool was ac-

curate—but premature. On June 13, a person with the AOL handle Duke121 wrote in the Diana “folder” of the Mot-

ley Fool that the company would take an \$850,000 writedown in its fourth quarter on the meat distribution business the company has been trying to sell. Without any other major news, Diana's stock slid 8% to close the day at 77½. And then, lo and behold, 12 days later the company reported fourth-quarter financial results—and they included an \$852,000

writedown. “That was clearly inside information,” says Diana Chairman Richard Y. Fisher. “We are going to look into how that got on the bulletin board.”

PURPORTED EXPERTS. At first glance, Diana is an unlikely company to find in the middle of an Internet controversy. Its primary business is distributing meat and seafood. What's driving interest in Diana is its 80% stake in Sattel Communications Corp., which makes switches aimed at lowering the cost of providing access to the Internet. The

“Reliable sources say that Diana's fourth quarter and yearend results will have much higher losses than previously expected.”

DUKE121

*On a Motley Fool message board,
June 13, 1996*

Motley Fool forum is full of messages from purported experts who expound in detail on Diana's technology. Since Diana's stock is thinly traded—only 4.1 million shares are outstanding—the stock is more prone than most to online influence.

What has been added to that mixture in Motley Fool are alarmist comments, both positive and negative. In February, a Fool forum participant with the handle VALUESPEC posted a public message saying that a “very bullish” announcement would come in the “not-too-distant” future. In March, the same

author wrote that “MCI might be interested in” Diana. The posters of these messages, who would not respond to E-mail queries from BUSINESS WEEK, an anonymous AOL subscribers. VALUESPEC describes him- or herself in a member profile as a 34-year-old owner of a landscaping business, while Duke121 will only disclose her gender and marital status.

Sometimes the online leads are correct, sometimes not. Diana did announce a major deal to sell 21 switches in May, which helped its stock rise even further. But no MCI Communications Corp.

interest has materialized. “I think the Motley Fool postings have definitely helped drive Diana through the stratosphere,” says Richard Keim, whose Keim Wilson Associates has a short position in the stock.

Since late May, the bears have had their way in the Motley Fool forum and with Diana. On May 29, Asensio & Co., a New York re-

search and trading firm, posted a recommendation on the Motley Fool bulletin board. The stock dropped 2½ to close at 101. The next day, “SsC prtr” posted a report that the Securities & Exchange Commission was looking into possible manipulation of



“There is talk of some big buyout of this company.”

BAITBOX

*On a Motley Fool message board,
Apr. 24, 1996*

Diana's stock—and the stock slipped another 2½. Fisher says he knows of no SEC investigation, and the SEC declined to comment.

The Diana saga shows that the Internet and online services are providing a new way to discuss securities: Anonymous people who may have hidden agendas can post any information they want, accurate or not, in a public forum. But perhaps less has changed than meets the eye. “The lesson is what it always been: Investigate before you invest,” says Merton Miller, a University of Chicago economist and Nobel prize winner. Even in the new world of cyberspace, the old lessons of investing apply.

By Peter Elstrom in Chicago



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BY GENE G. MARCIAL

THIS DRUG DEAL MAY BE ON AGAIN

A takeover of Allergan (AGN) was almost in the bag in early May, until Volvo blocked the acquisition—by drug-maker Pharmacia & Upjohn, of which the carmaker owns 14%. Now, it seems this maker of eye-care products and pharmaceuticals is back in play.

Volvo has suddenly announced it is selling the bulk of its P&U holdings. "That removes the impediment to an Allergan buyout," says Bob Willens, managing partner at Lehman Brothers. He expects P&U will try again.

Volvo opposed the deal: It was based on a stock-for-stock pooling of interests, an accounting treatment that does not allow inclusion of goodwill in the deal. If a big stakeholder such as Volvo sold shares up to 30 days before the closing or 90 days thereafter, such a merger would be disallowed. Now that Volvo has registered with the Securities & Exchange Commission to sell 70% of its shares in late July, cutting its stake to less than 5%, the deal can go on, notes Willens, who thinks Allergan is now a good play. The sale should bring Volvo \$1.6 billion.

HOT NEW REMEDIES IN SIGHT



Now trading around 40, Allergan is undervalued, says a manager at a New York firm that invests solely in health-care issues. This pro figures the stock is worth 50 to 60 in a buyout. Volvo's withdrawal "is really the precursor to P&U's takeover of Allergan," he says.

Even with no takeover, Allergan stock is cheap, says Oppenheimer's Steve Gerber. Allergan's "continuing appeal" is its new-product flow, he argues. Allergan has produced new retinoid drugs—including Zorac for the

treatment of psoriasis and acne, which Gerber thinks will get the FDA nod this year. "It has the potential to become Allergan's biggest product, with annual sales exceeding \$100 million," he says.

Another Allergan product, Alphagan, a topical glaucoma therapy, has a good chance of FDA approval by next year and could "rejuvenate the company's important franchise in the glaucoma market," says Gerber.

IS SPACEHAB SET TO SOAR?

Shares of Spacehab (SPAB), the first company to develop and operate habitable modules aboard the U.S. Space Shuttle, remain firmly earth-bound. Spacehab went public on Dec. 20, 1995, at 12. They're now at 10, down from 15 in early April. No matter, say some of Spacehab's almost cultish following. They're buying for one reason: They foresee NASA privatizing much of the space program, which would boost demand for Spacehab's services.

"It's the only company of its kind—a pure play on the commercialization of space," argues investment manager Renee Carret of Carret & Co., a New York firm. "You're buying a unique company on the cheap." She expects earnings of \$1.50 a share this year.

With several companies, such as Eli Lilly and Schering-Plough, and other researchers performing experiments on Spacehab's labs, Carret expects it will form alliances with one or two drug or chemical companies. Formed in 1984, Spacehab developed modules for efficient use of the Shuttle's cargo bay. The company operates a payload processing facility next to NASA's Kennedy Space Center at Cape Canaveral, Fla. McDonnell Douglas, which owns about 3% of Spacehab, designs and produces the Spacehab modules and prepares them for flight.

One New York money manager is betting McDonnell Douglas will form a joint venture with Spacehab to widen its share of the payload processing and servicing of the Shuttle. Morty Schaja, managing partner at Baron Capital Management, which owns 4.8% of Spacehab, says the stock is undervalued based on earnings, "which could grow significantly over the next three years." He sees the stock doubling in that period.

ONE MAN'S 'WAY TO WIN'

When Zurich Insurance bought Kemper, a Chicago financial-services outfit, last January, Kemper COO Steve Timbers expected the buyers to impose a defensive posture. But they didn't. "Zurich bought us for what we were—including our investment style," he says. "The way to win is to combine value and growth strategies."

Timbers, now president of Zurich Kemper Investments, is high on three stocks: Paging Network, Marriott International, and MBIA. All of them have strong finances, fast-growing earnings, and low price-earnings ratios.



TIMBERS: He hunts for value

Dominant in wireless communications, Paging Network (PAGE) has expanded fast. Yet its stock, at 21, trades at a depressed p-e despite its 50% growth rate. Timbers expects Paging's VoiceNow to be a blockbuster. VoiceNow uses common pager and cellular technology to create a portable answering machine.

Marriott (MAR) is benefiting from the lack of new hotel building and the cyclical upturn in bookings, says Timbers. One of Marriott's assets with huge potential is its Senior Living Services unit, which caters to retired people. Marriott plans to expand this unit into a larger home health-care operation and possibly spin it off or take it public.

MBIA (MBI) is the leader in municipal-bond insurance. Timbers thinks the pace of bond offerings will rise—after two slow years. He notes that MBIA has "superior franchise, balance sheet, and management." At 74, the shares are "unbelievably cheap," he says, based on estimated earnings of \$7.10 a share in 1996 and \$7.80 next year.

Tips from Timbers

	STOCK PRICE	52-WK HIGH	TARGET PRICE
PAGING NETWORK	21	28	33
MARRIOTT INTL.	49	51	60
MBIA	74	80	103

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TELECOMMUNICATIONS

READY, SET, DEVOUR?

AT&T wants to grab a third of the regional-calling market in a few years

It's the telecom world's version of a war council. Every week or so, about 15 AT&T executives meet at the company's Basking Ridge (N.J.) headquarters to discuss the latest maneuvers by the company and its opponents in the battle for a \$90 billion prize—local calling. The team, which has dubbed itself "Mission Control," was formed almost two years ago, but the members shifted into high gear in February. That's when the Telecommunications Act of 1996 became law and local calling markets were thrown open to competition.

Now, Mission Control is hopping. Headed by President Alex J. Mandl, the team has laid plans for AT&T to get into local calling in every state by the end of 1997, with trials starting in five states on Sept. 1. AT&T Chairman Robert E. Allen spelled out his ambitions in the new market in a speech to investors on June 11: "We plan to take at least a third of the local market within a few years," he declared. Mandl says that AT&T not only will hit Allen's target but will also break even on local service in two to three years.

MISSION "IMPLAUSIBLE." Industry analysts aren't so sure. The only immediate path to local calling is to buy service from a regional phone company and resell it. That makes it unprofitable to offer deep discounts, the easiest way to grab customers from the entrenched former monopolies. "The economics of local resale simply can't yield such large market share gains," says Scott Cleland, an analyst with the Washington Research Group, who terms Allen's goal "implausible."

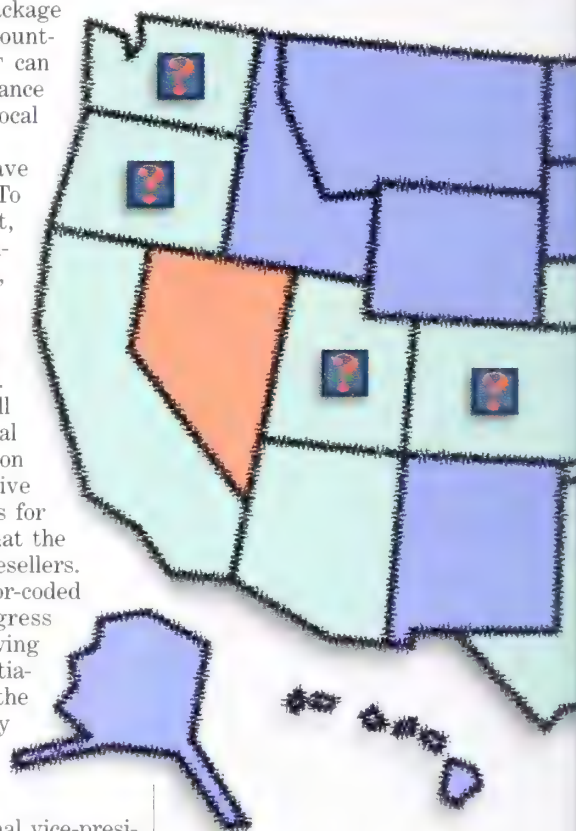
There is one simple solution: sell local service as a loss leader. Like other phone companies in the deregulated market, AT&T plans to compete by offering a bundle of telecom services—local, long-distance, and cellular calling, plus data and video ser-

vices. AT&T isn't discussing how it will price local service or its bundling plans. But says Shaun P. Gilmore, AT&T's Northeast states president: "The local-services part of a package of services could be discounted." In other words, AT&T can use profits from long-distance or satellite TV to pay for local discounts.

But first AT&T must have local service to offer. To come up with a product, AT&T is developing a complex strategy of reselling, partnering, and building its own facilities—both wired and wireless connections to homes and businesses. At the start, the mix will depend on state and federal regulators, who must rule on a huge range of competitive issues, including guidelines for the wholesale discounts that the local carriers must offer resellers.

At Mission Control, color-coded maps depict AT&T's progress across the country—showing the status of resale negotiations in every state and the discounts determined by state regulators so far. The team also scrutinizes regular progress reports from the seven new regional vice-presidents. Right now, the focus is on California, Georgia, Illinois, Michigan, and Connecticut, where local trials begin on Sept. 1.

MAPPING OUT THE BATTLE



THE COST OF CALLS

AT&T will enter the local calling market by reselling service it buys from the regional phone companies. So far, state regulators have settled on the following wholesale discounts to be offered to resellers:

CALIFORNIA

PACIFIC TELESIS
17% residential direct
19% business direct

GTE

12% residential direct
17% business direct

COLORADO

9% residential direct
16% business direct

CONNECTICUT

54% residential direct
(above the retail price)



BUGGING THE BELLS: AT&T discounts will pressure local carriers

Take a shortcut to savings.

So the folks in Basking Ridge are ring over reams of data on the buying bits of their 80 million residential customers. AT&T figures it can use the information collected from its long-dis-

side, resisting every effort to interconnect to our network," he says. "I have the world's record for losing those same arguments from '68 on." Zeglis figures the company will end up in arbitration in all 50 states, and based on his own lack of success with arbitrators back in AT&T's monopoly days, he's confident that the Bells will lose every time. For their part, Bell executives routinely accuse AT&T of dragging out the negotiations in order to score points with regulators. The long-distance giant says the local phone companies aren't budging from unacceptable discount offers. "Our job is to create an environment that's conducive to competition—not to subsidize our competitor," snaps Ameritech Corp. Chairman Richard C. Notebeart.

ALL IN ONE. Long term, AT&T says it would just as soon control its own local networks. The cost of building is staggering. Constructing "local loops" in the top 50 markets could cost upwards of \$5 billion, industry analysts estimate. AT&T does plan to build facilities in the largest markets and has already started in Los Angeles, Chicago, and New York. For the rest of the country, "we want to use other people's assets and capital everywhere we can," says Harry S. Bennett, vice-president of AT&T's Local Services Div. Bennett says AT&T will partner with cable operators, competitive access providers (CAPs) that serve businesses with private lines, and even electric utilities. It already has contracted with five CAPs that serve 70 cities.

The other local play is wireless. AT&T spent \$12 billion two years ago to buy McCaw, the nation's largest wireless calling operator. It is converting that network from analog to digital and is building a nationwide wireless network based on all-digital personal communications services (PCS) technology. By late 1997 or early 1998, says Bennett, 80% of the country will be covered by an all-digital AT&T Wireless network. At that point it might be viable to offer wireless as a local-service alternative.

Ultimately, AT&T wants to offer any and all of these options. It can't afford not to. The Baby Bells are all gearing up to enter long distance—and other services including cable TV—and AT&T figures the best way to hang on to its existing customers is to sell them a lot more. "All of our market research shows that the customer prefers to have local and long distance treated as one," says Mandl. Expect a lot of late nights for the Mission Control team if they want AT&T to be the one.

By Catherine Arnst in Basking Ridge, N. J., with bureau reports

AT&T'S NEW BOUNDARIES IN CYBERSPACE

The AT&T executives trying to push into local calling have one thing to be happy about. As tough as their job is, it's unlikely ever to be as frustrating as the company's efforts in cyberspace.

AT&T has spent millions to launch—and then kill—several online initiatives. Like many companies, it hoped to create proprietary services

access to cellular calling and satellite TV. AT&T's primary thrust will be signing millions of customers for WorldNet, its new Internet service. To help its 10 million business customers get wired, AT&T will also provide a "hosting" service called EasyCommerce, which will create and run corporate Web sites. These businesses are "a clear extension of AT&T's telephony

MANZI
Industry.Net's boss will fold AT&T's New Media Services into a new company that will be the "home page for business"



and charge a premium for them. But the Internet changed all that. Now, the company is cleaning out the last bits of its old cyberstrategy and narrowing its focus to providing Internet access to consumers and businesses—which it sees as part of basic telecom service in the future. "AT&T is severing its ties with everything outside of its core business," says Blane Erwin, an analyst with Forrester Research Inc.

PARTIAL RETREAT. So on June 24, the company took the ax to New Media Services, a publishing unit that includes what's left of Interchange, an online service that it bought in 1994. The unit will be spun off to Industry.Net, the company headed by former Lotus Development Corp. chief Jim P. Manzi that runs a Web marketplace for business. The combined company, Nets Inc., in which AT&T gets a minority stake, will use content developed for AT&T Business Network, a Web site. It will be, says Manzi, "the home page for business."

Is AT&T giving up? Hardly. The Net is a critical part of its plans to be a one-stop shop for electronic communications—from E-mail and Internet ac-

cess to cellular calling and satellite TV. AT&T's primary thrust will be signing millions of customers for WorldNet, its new Internet service. To help its 10 million business customers get wired, AT&T will also provide a "hosting" service called EasyCommerce, which will create and run corporate Web sites. These businesses are "a clear extension of AT&T's telephony

business," says Michael E. Kolowich, president of AT&T New Media, who will become vice-president of business operations for Nets Inc. Indeed, the Internet may be evolving to become a lot more like the phone business. In the past year, AT&T's revenue from 800 calls surpassed that from long-distance service, says Kolowich. The same model is taking shape on the Net: Just as companies are willing to foot the bill for an 800 number to bring in business, they are willing to pay for the costs of Web sites and advertisements to lure customers. AT&T is betting those 800 customers are ripe for the EasyCommerce Service.

What else doesn't fit in AT&T's new online plan? The company has already scrapped Network Notes, a proprietary business network and is looking to get rid of the Imagination Network, an online gaming setup. Personalink, a messaging service using technology from General Magic Inc., may be phased out. And Kolowich says AT&T is seeking partners to take over its consumer content, too. What's left may be just the ticket for a New Age phone giant.

By Amy Cortese in New York

WILL THE DELTA CLIPPER SCUTTLE THE SHUTTLE?

ASA hopes it will bring launch costs down to earth

In 1990, the Pentagon's Star Wars program called for a radically new rocket that would do what no other spacecraft had done: climb into orbit in a piece, without dropping off booster rockets on the way up—and without a man pilot on board. It would be the space equivalent of an airliner—reusable and therefore cheaper to operate.

Skeptics at NASA insisted that any rocket big enough to hold all the fuel required would be too heavy to reach orbit. But aerospace companies crunched the numbers and decided a so-called single-stage-to-orbit (SSTO) rocket had come technically feasible. McDonnell Douglas Corp. won the contest to build a suborbital vehicle to test the concept. Today, its rocket—the Delta Clipper Experimental, or DC-X—is one of three contenders being evaluated by NASA as a potential successor to the space shuttle.

A decision should come on July 1.

Despite the skepticism, NASA has embraced the one-piece approach since inheriting the DC-X program from the Pentagon last year. On June 7, after watching the 10th test flight since 1993, NASA Chief Daniel S. Goldin left no doubt at the fate of NASA's longtime pet, the space shuttle.

"This is how we will change space flight," he told the crowd gathered at White Sands Missile Range in New Mexico.

W FRONTIERS. The main goal is to open the tab for lifting payloads into space to only 10% of current costs, which run about \$10,000 per pound. The U.S. space-launch industry would then have by far the lowest-cost launcher and might be able to recapture some of the 70% market share it has lost to rivals in France, Russia, and China. Cheap access to space could also usher

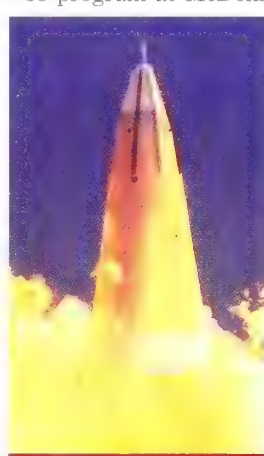
in a new economic frontier, just as "railroads opened up the West," says Paul L. Klevatt, who directed the McDonnell Douglas DC-X team.

Goldin's determination to replace the shuttle doesn't necessarily mean its successor will resemble the pyramid-shaped DC-X. The McDonnell Douglas design could get whipped by sleek rivals with winglets. Both Lockheed Martin Corp. and Rockwell International Corp. have offered less risky SSTO designs that would take off vertically but land horizontally, like the shuttle (table).

For the winner, there's a prize of \$900 million, over three years, to build a half-size experimental model. This experimental vehicle, to be called the X-33, will be used to test the technologies needed for a full-fledged reusable launch vehicle—RLV, for short.

The next step is to prove that an SSTO rocket can actually be light enough and powerful enough to reach orbit. That requires a host of new technologies, says Payton. Some progress has already been made with the DC-X, earning it a new moniker: DC-X Advanced, or DC-XA. For example, the fuel tank that holds liquid hydrogen is now made from graphite-epoxy composite. It tips the scale at 2,146 pounds, or 66% less than its aluminum predecessor.

Still, there's no way the DC-XA could fly fast enough to leave the earth's gravity, says Klevatt, who now runs the X-33 program at McDonnell Douglas. Big-



THE DC-X LIFTS OFF

ger engines and a lighter, all-composites structure are needed to attain the "escape velocity" of 17,500 miles per hour. These improvements will be tested in a DC-XA spinoff, if McDonnell Douglas wins the X-33 job.

NASA funding will stop in 1999, however.

The agency wants the winner to pick up the multibillion-dollar cost of building the full-size RLV. **TOURISM.** All three contenders are cautiously optimistic that they can raise the money. But a successful X-33 is a crucial first step, says Thomas K. "T.K." Mattingly, Lockheed Martin's vice-president of reusable launch ve-

hicles. Without solid proof from the X-33 that the single-stage-to-orbit idea is feasible, "we think it would be impossible to attract the necessary capital," Mattingly says.

If there are no major hitches, improved second-generation RLVs might trim launch costs to \$300 per pound or less. Even space tourism could then be affordable. But Klevatt figures you'll probably have to wait until 2012 to dash off for a weekend in orbit.

By Otis Port in New York and John Carey in Washington

REUSABLE LAUNCH VEHICLE CONTENDERS

SPACECRAFT FEATURES	LOCKHEED MARTIN	McDONNELL DOUGLAS	ROCKWELL INTERNATIONAL
TAKEOFF AND LANDING	Vertical, horizontal	Vertical, vertical	Vertical, horizontal
HEIGHT AND WINGSPAN	127 ft. long, 123-ft. wingspan	185 ft. long, no wings	213 ft. long, 103-ft. wingspan
DEVELOPMENT COST	\$4.5-\$5 billion	\$4-\$7 billion	\$5-\$8 billion
PER-POUND LAUNCH COST	\$1,000	Under \$1,000	Under \$1,000

DATA COMPANIES

There are two crucial steps in the development of an RLV, says Gary E. Payton, manager of NASA's reusable launch vehicle program. One is to slash operating costs by eliminating the small army that NASA needs to service the shuttle and strap on its external main engine and booster rockets. That's the reason for packaging everything into one single-stage rocket that can be serviced as easily as an airliner, Payton notes. In June, a 24-person ground crew was able to relaunch the 42-foot-tall DC-X 26 hours after it landed.

Premiere in Monte Carlo.



MILAN



MONTEGO



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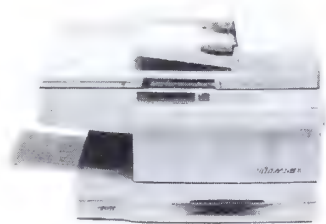
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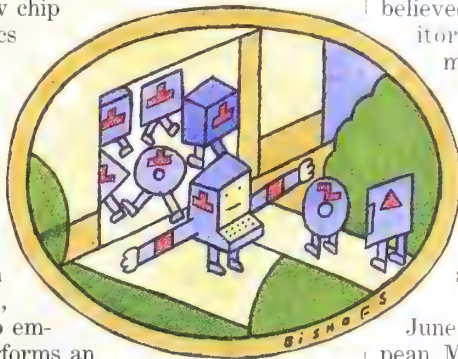
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LOCKING IN BRAND LOYALTY

MAKERS OF LAPTOPS, CELL PHONES, AND OTHER CONSUMER gear want users to stick with their brands when they buy add-ons such as battery packs or expansion cards. It's a way to ensure quality, manufacturers say. It also lets them charge a premium for accessories.

Next month, their mission could get a lot easier, thanks to a new chip from EXEL Microelectronics Inc., a San Jose (Calif.) subsidiary of Japan's Rohm Co. EXEL's new chip uses the same "challenge-and-response" encryption tricks that Net surfers use to protect E-mail. When a new battery is plugged into an EXEL-protected cell phone, for example, an EXEL chip embedded in the battery performs an electronic "handshake" with a corresponding chip in the phone. In that handshake, the phone chip issues a random, 32-bit number to the battery chip, which combines that number with a longer, 64-bit "key," and bounces it back to the phone. If the new number doesn't match a similarly calculated number in the cell phone, the battery is rejected. Bad news for consumers, perhaps, but good news for manufacturers. □



STRESS PROTEINS: AN IMMUNE-SYSTEM MYSTERY UNFOLDS

WHEN ASSAULTED BY HEAT OR pathogens, most organisms produce "stress proteins"—mysterious molecules believed to be crucial in monitoring cell health and maintaining immune responses. Scientists are beginning to understand how they work and may soon harness them to fight AIDS, cancer, and some hereditary ailments.

In a report in the June 17 issue of the European Molecular Biology Organization's *EMBO* journal, Richard I. Morimoto, a molecular biologist at Northwestern University, reports that two stress proteins called HSP 90 and HSP 70 help to make sure that certain other proteins in a cell are folded into the proper configuration. Ab-

normalities in folding are implicated in such human ailments as Creutzfeldt-Jakob disease, the human analog of mad cow disease.

Morimoto's report complements an earlier announcement from the Whitehead Institute for Biomedical Research in Cambridge, Mass. Collaborating with StressGen Biotechnologies Corp.—a biotech startup in Victoria, B.C.—Whitehead scientists injected mice with a genetically engineered vaccine made of stress proteins and purified HIV viral proteins. Later, when the mice were infected with whole HIV viruses, they were able to fight the infection.

StressGen wants to develop such mixed-protein vaccines for a variety of diseases. It is also developing cancer therapies. By injecting stress proteins into mouse tumors, StressGen scientists hope to make the animals' immune systems recognize and destroy the tumors. □

INNOVATIONS

In late-stage prostate cancer, rapidly multiplying tumors can shatter bone, causing intense pain. In two clinical trials Novantrone, a chemotherapy drug for leukemia developed by Seattle-based Immunex Corp., has been shown to kill the cells and bring temporary relief. Immunex is seeking for speedy Food & Drug Administration approval for prostate cases.

Japan dominates in flat-panel displays, making it tough for non-Japanese speakers to pick the technology. They'll soon have help. Interlingua, a translation firm in Redondo Beach, Calif., plans to post English versions of Japanese magazine articles and government documents on the Web (<http://www.japanese-translation.com>). The access fee: a flat \$100 per hour.

THE ELM MAKES A COMEBACK

AMERICA IS SLOWLY WAKING UP FROM THE NIGHTMARE on Elm Street—the onslaught of Dutch elm disease that began in the 1930s and wiped out 90% of American elms. After more than 20 years of effort, the U.S. Agriculture Dept.'s National Arboretum has identified two varieties of American elm that are unusually resistant.

The work was more high-patience than high-tech. Plant geneticist Alden M. Townsend (photo) and his retired colleague, Lawrence R. Schreiber, took cuttings from healthy elms and grew thousands of trees, then injected them with the *Ophiostoma ulmi* fungus. The Valley Forge variety was first in resistance and New Harmony second, ahead of the popular Liberty that's distributed by the Elm Research Institute of Harrisville, N.H. (The institute says its elm has a longer record of success.)

Now it's elm lovers who must be patient. The trees won't hit nurseries until 1999 and won't reach full height until 2050. And we may never again see majestic rows of elms—it's bad practice to plant them close together because their roots graft and transmit diseases.

Peter Coy



FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwjul@businessweek.com

TACTICS

BILL'S FIRST-STRIKE TV BLITZ

Clinton may already have spent \$15 million—and it's paying off

To Denver TV viewers, the ads are becoming as familiar as the faces of Alex Trebek and Vanna White. Sometimes squeezed between *Jeopardy* and *Wheel of Fortune*, an image appears: a dour-looking Bob Dole in grainy black and white. A somber voice intones that the Republican standard-bearer voted no on everything from Medicare to the environment. Dissolve to a pink-cheeked President Clinton on a podium. His budget protects education, health care, and kids, viewers are assured. Cut to a happy couple holding a baby as the announcer declares: "It's time to say yes to America's families."

Summer has just arrived, but Denver and other selected U.S. cities have been bombarded for months by hundreds of reelection messages sponsored by the folks who bring you Bill Clinton. The Clintonites are in the midst of the biggest—and earliest—broadcast assault in the annals of Presidential politics.

Between Mar. 1 and June 14, the Democratic National Committee and Clinton's reelection committee ran more than 17,000 spots, according to National Media Inc., a Republican media consultant which tracks political advertising.

ELECTION '96

(The DNC and the Clinton campaign won't discuss details of their media buys.)

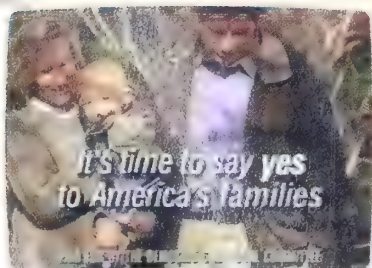
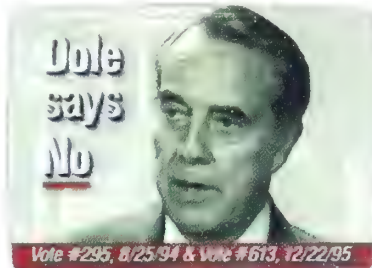
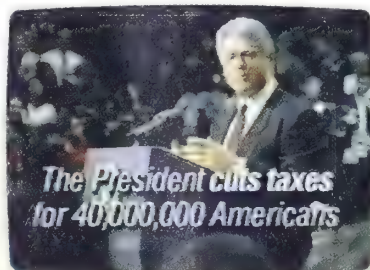
The spots are playing in 50 mostly medium-size markets in 25 states—far from the eyes of Beltway pundits. The cost: about \$15 million so far this year, with possibly \$100 million spent by November, far more than in '92.

Clintonites began plotting their early media campaign last summer, when they realized the GOP Presidential nomination would probably be decided by late March and voters could start making up their minds. So the President's team set out to co-opt popular Republican issues, such as crime and welfare reform, and to deflect attention from GOP causes like tax cuts. Using polls that showed

voters liked Clinton's defense of Medicare, student loans, and the environment, strategists decided to hammer Dole at these points. "Initial political impressions can be very persuasive," says Ann Lew, deputy campaign manager, who notes that the ads enable Clinton to take a positive message directly to the people. **OFF GUARD.** Now Dole is playing catch up. A cash crunch delayed a strong rebuttal from the Dole camp, caught off guard by the immensity of the Clinton blitz. Though the GOP placed some early ads, only now is the Republican National Committee unleashing its own \$15 million media campaign, with ads lambasting Clinton for vetoing welfare reform bills and for his 1993 tax increase. But says Robert P. Leone, professor of marketing at Ohio State University, "Clinton has had the advantage of defining the terms in an uncluttered environment." Now, he says, Dole "has to convince me that what I have heard in two months isn't true."

The ads are aimed at swing voters, and their placement provides a road map to the President's electoral strategy. He's focusing on small and midsize cities like Fresno, Calif.; Wilkes-Barre, Pa.; Raleigh, N.C.; Green Bay, Wis.; and Toledo—all home to blue-collar Reagan Democrats. They're also targeting suburban communities such as Orlando and Grand Rapids that lean Republican but are Democratic "persuadables." An

TARGETING SWING VOTERS



Number of times this Clinton commercial was broadcast, 3/1/96 to 6/15/96, by market

● 0-50 ● 51-100 ● 101-150 ● 151-200

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New technologies

New purchase influencers

New opportunities

New informational needs

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Clinton hopes to retain his lead among women by emphasizing family issues.

The Clintonites are avoiding states the President has little chance of winning (Utah and Alabama) and those already in the bag (New York). Although the GOP has the edge in the South, Clinton believes he can repeat his 1992 victories in Georgia, Kentucky, and Tennessee. And he's buying heavily in Florida and North Carolina, states he lost by close margins in '92. In the targeted markets, the ads are airing on a gamut of shows, from CBS's *Sunday Morning* to tabloid TV like *Inside Edition* to daytime talk shows like *Live with Regis & Kathie Lee*.

White House strategists attribute Clinton's lead in the polls in part to the TV campaign. Although it's hard to isolate the ads' direct impact, changes have been dramatic in some states that have been bombarded. In Connecticut, Clinton's lead soared by 20 points between early March and early June. But in Michigan, which will be one of the hardest-fought states this fall, the ads have barely budged the President's job approval ratings, in the low 50s for months. But they're keeping him from losing support because of negative publicity, such as the Whitewater investigation and GOP attacks. Says Lansing (Mich.) independent pollster Ed Sarpolus: "They're neutralizing some of the hits."

TUNE OUT. Jay Schulberg, chief creative officer of Bozell Worldwide, a New York ad agency, says the spots are important because they bolster Clinton's image as a President standing firm. "There's a subconscious association of [Clinton] as a good product and good brand," he says. "By having a strong and positive presence month after month, people will tend to overlook momentary problems."

But the Denver ads haven't won over everyone. Says Elwin E. Shaklee, a locksmith who describes himself as conservative: "They haven't changed my mind about him. They've cheapened him."

A sustained marketing campaign also risks causing voters to tune out. Moreover, Alex Castellanos, a Republican media consultant and principal at National Media, says that Clinton, by portraying himself in the ads as father-protector, "has to become something he's not, and that's hard to sustain."

But the President's media strategists are betting that if they make their case enough times, voters will go for a new and improved Bill Clinton, even if they don't buy the whole pitch. That means the couch potatoes of America may be hearing a lot more from the Pitchman-in-Chief as the campaign unfolds.

By Susan B. Garland, with Richard S. Dunham in Washington and Sandra Dallas in Denver

Marketing

CATALOGS

LANDS' END LOOKS FOR TERRA FIRMA

The cataloger moves back to basics. Is its strategy solid?

It was a blustery December day in tiny Dodgeville, Wis., 18 months ago, and young Michael J. Smith got the kind of break most people only dream about. The 34-year-old had been named CEO of Lands' End Inc., the \$1 billion catalog giant, leapfrogging a host of more experienced executives. The previous CEO, William T. End, had just been shown the door by Gary C. Comer, the company's charismatic founder and largest shareholder, for pushing too far, too fast into new ventures. Smith's charge from Comer: Take Lands'

End back to its roots—providing high-quality, classic apparel and the best customer service in the business.

UGLY DEBUT. The opportunity was great, but the timing couldn't have been worse. Smith, who had been head of Lands' End's Coming Home specialty catalog, was handed the reins just as Lands' End was heading for the toughest year in the fast-growing company's 33-year history. With little warning last year, paper prices doubled and apparel demand collapsed. A postal-rate increase added to the pain, slashing the company's third-quarter profits by 60%. Embattled on all sides, Smith had to cut back mailings to save money. Lands' End finished the year with profits down 15%, to \$30.6 million, on sales of \$1 billion. There have been other obstacles as well. With two former CEOs on Lands' End's board, including the founder, Smith has had to fight the perception that he's merely a figurehead. He has also had to cope with the loss of three top executives who left after his appointment.

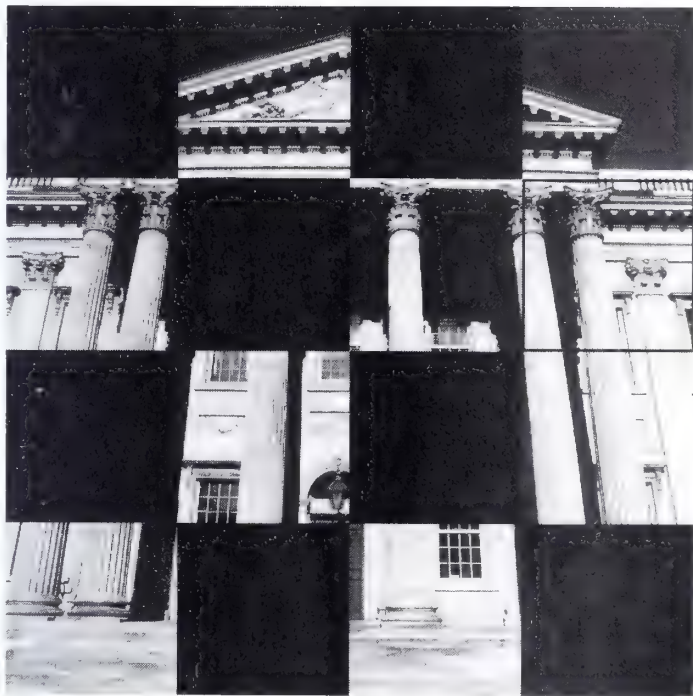


CEO SMITH: Fighting the perception that he's a figurehead

A lot of CEOs might have panicked after such an ugly debut. But Smith, who joined the cataloger as a market-research analyst in 1983 straight out of the University of Wisconsin, is as unflappable as a Lands' End button-down shirt. Instead of trying to save money by cheapening products or slashing head count, Smith has done the opposite: spending to improve quality and increase employee benefits. It's a marketing-driven decision. "Our customers will pay for great-quality products" sold by employees who could handle them, Smith says. And why not? The average customer is a college-educated baby boomer with a median household income of \$60,000.

Intoning the words of Chairman Comer, who started a catalog for sailing gear in 1963 ("Make it as good as you can. Improve it whenever possible"), Smith went to work refining Lands' End classics, making seams on mesh knit shirts stronger and adding fleece to the pocket

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Sun designed the first intranet back when people thought intranet was a typo.



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squall jackets. When staffers told him Lands' End's top-selling children's snow jacket wasn't really waterproof, Smith pulled it from the catalog in early 1995, replacing the company with \$500,000 in inventory. And when some customers received defective turtlenecks, Smith sent 10,000 letters of apology and offered replacements.

Laying off workers would have been the fastest way to boost the cataloger's sagging bottom line. But instead of chopping any of Lands' End's 5,400 jobs, Smith is adding benefits such as adoption assistance and mental-health referrals. Part-time employees already receive full health-care benefits. Why the generosity during tough times? "If people feel squeezed, they won't treat the customer well," Smith says. Although it's too early to say if Smith's strategy is working, last-quarter profits were more than tripled, to \$4 million, compared with the year-ago period, thanks to fewer markdowns and higher sales per page from the men's and kids' specialty catalogs. Sales for the period rose 2.3%, to \$1.1 billion. David P. Ricci, an analyst at William Blair & Co. in Chicago, has a "buy" on Lands' End stock, even though it's already up more than 85% this year, just under \$24 a share.

It's still about 14% below its 1994 high of almost \$28. Investors such as Steve M. Wilson, with New York money manager Reich & Tang Asset Management, say they like Smith's quality drive. "They're doing what they're supposed to—getting back to basics," says Wilson, whose firm owns about 3% of Lands' End stock. Almost 60% of Lands' End shares are controlled by insiders, with Smith, now 68, holding 53%.

AGING PROBLEM. While Smith's quality drive may preserve the core business, critics say it could also doom the company to slow growth and a declining return on investment. In the past five years, Lands' End's growth hasn't come from the core catalog. Instead, it has come from acquisitions, international expansion, and new specialty catalogs. Since 1991, those new ventures have grown one-third of the company's \$1 billion in annual sales. Meanwhile, sales through the main catalog, which is mailed 12 times a year, have been almost flat.

Nevertheless, that's where Smith is focusing. International expansion and further acquisitions? They're on hold. The same for spin-offs, such as catalogs for large women and petites, which retail experts say are a natural.

But by concentrating on the main book, Smith runs the risk of being left behind, especially overseas. The company, which entered Britain in 1991 and Japan in 1994, is only now venturing into Germany despite a successful market test two years ago. Its former head of international sales, William J. O'Neill, resigned a year ago after losing a battle to speed up expansion abroad. "My biggest issue with them is pace. It's been too slow," gripes Dean Ramos, retail analyst with Dain Bosworth in Minneapolis. Meanwhile, competitor Eddie Bauer Inc., a unit of Spiegel Inc., launched its own free-standing German catalog in 1994 and plans to open three Eddie Bauer stores in Germany in the fall. Smith says he's comfortable with the current pace of international growth. "You have to prioritize and make choices," he says.

Smith has another battle—convincing people he's really in charge. Both Comer and former CEO Richard C. Anderson sit on the six-person board. Smith's youth and the abrupt departure of William End, an L.L. Bean Inc. veteran recruited by Comer in 1991, left many wondering if Comer and Anderson had decided to call the shots themselves. "Bill End was a more independent executive. Smith is cast in the mold they created," says catalog consultant Maxwell Sroge. Anderson and Comer declined to comment on their roles.

Smith, who wears only Lands' End duds and drives a 1989 Honda Accord despite his \$306,000-a-year salary, insists he's in charge. He says he asked Anderson to come in once a month after the 1995 departure of Philip J. Iosca—a respected merchandising executive and Smith's former boss who left to head up kids cataloger Hanna Andersson Corp. Smith has certainly shown he can protect the Lands' End franchise. The question is, can he make it grow again?

By Susan Chandler
in Dodgeville, Wis.



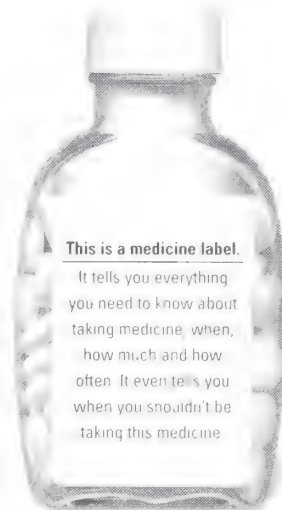
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EDITED BY AMY DUNKIN

BACK FROM THE DEAD: LIMITED PARTNERSHIPS

Surprise! The once moribund market for publicly registered limited partnerships has perked up. The recovering real estate sector, where more than half of these disastrous deals were done, has brought new life to this group of widely promoted investments of the 1980s.

INVESTING

"You couldn't give away some of these partnerships three years ago," says Spencer Jefferies, the Dallas publisher of *Partnership Profiles*, a directory and newsletter of partnerships. Not anymore. Such investments, which are long-term instruments giving buyers ownership interests in assets such as real estate and oil and gas, are still being sold for much less than what the original investors paid for them. They generally sell at a 20%-to-60% discount to net asset value. But recently, prices for many of the real estate deals have more than doubled.

Take Balcor Realty Investors 85-2, a portfolio of apartment buildings originally sold in 1985 at \$1,000 a unit. In June, 1993, partnership units were selling for \$44, according to James Frith Jr., president of Chicago Partnership Board, the largest of the firms that trade limited partnerships in the secondary market. Early last month, units sold for \$329 apiece.

GOT STUCK. This is welcome news for the estimated 10 million buyers who gobbled up \$130 billion worth of the limited partnerships when real estate was booming and oil and gas prices were strong. Lured by tax breaks that allowed deductions

of limited-partnership losses from ordinary income, investors watched that advantage disappear along with the Tax Reform Act of 1986. Gross mismanagement, high fees and debt, and a severe real estate recession further harmed many of the partnerships.

Unfortunately, investors were stuck. Limited partnerships weren't designed to be traded. Of the 2,000 partnerships, only about 300 trade with regularity—and then only at independent dealers that have established their own clearinghouses for such transactions, yet offer no guarantees that sellers are getting the best prices. But trading volume jumped from \$100 million in 1993 to \$200 million last year, and that upward trend is expected to continue, according to Jefferies of *Partnership Profiles*.

What's driving the increased trading activity? Liquidations, in part. More investors are jumping into the secondary market because there is a definitive time frame for investment returns on dissolving partnerships. Some sponsors see the improving real estate market as the long-awaited opportunity to cash out. Merrill Lynch, for instance, has already liquidated three of the six MLH Income Realty partnerships its brokers hawked to clients. "Brokerage houses are anxious just to get out of the market," says Ross T. Bowler, a secondary market maker in Madison, Wis. These deals left them awash with expensive shareholder lawsuits and hefty fines levied by the Securities & Exchange Commission for improper sales

practices. But careful investors have lately been noting that, while the selling techniques often may have been shoddy, many of the properties are still valuable.

Indeed, when these properties are sold and the proceeds are paid out to unit holders, it can mean huge capital gains. Consider MLH II, an apartment-building deal sold by Merrill Lynch in 1985 at \$1,000 a unit. In July, 1995, a unit sold for \$105.63 in the secondary market. Two months later, Merrill Lynch liquidated the assets and paid investors \$179 per unit. That's a 66% return in just two months. Add that to the cash distributions, and these quirky little deals can make

attractive buying opportunities—but only for the sophisticated investor who avoids highly leveraged partnerships and is willing to plow through financial statements to study the market.

Locating information and evaluating it to determine how much the units are worth is tough. "This is the used-car market, not the New York Stock Exchange," warns Glen Bigelow, a portfolio manager in New York. **IN THE BALLPARK.** It's getting easier, though. The Chicago Partnership Board launched a free Web site (<http://www.cpbboard.com>) that reports units available for purchase, most recent prices and other data. The site also has partnerships' financials. Or you can call Disclosure Inc. (800 638-8241) to get annual reports, 10-Ks, and 10-Ks. Pricing is also available from Robert A. Stanger & Co., which tracks limited partnerships for \$5 a minute (900 786-9600). And federal approval is pending for the National Association of Sec-

What to Consider Before Buying

Despite the lure of high yields and possibly hefty capital gains if a portfolio is liquidated, sophisticated investors should weigh the following points before delving into publicly registered limited partnerships.

GENERAL PARTNER OR SPONSOR Go for brand names such as PaineWebber, Balcor (American Express), Merrill Lynch Hubbard (MLH), JMB Realty, Cigna, and T. Rowe Price. Look for deals where sponsors sold partnerships to their own clients, as with those conceived by brokerage firms and insurance companies.

LIQUIDATION HORIZON Many partnerships, such as Merrill Lynch Hubbard and Dean Witter, are liquidating, and more will follow. It's best to stay with these deals, since you know how long your money will be tied up.

TYPE OF PROPERTIES Miniwarehouses and apartment buildings are hot. Skip older office buildings. Unleveraged properties are less risky.

CASH DISTRIBUTION Stick with partnerships that have solid cash payout histories.

YIELD The higher the yield, the lower the discount. Most yields range from 8.5% to 11%.

DATA BUSINESS WEEK

ies Dealers' plan to list limited-partnership quotes on its electronic OTC Bulletin Board. Armed with the financials, you can do some basic research. For a ballpark estimate on an unleveraged real estate unit's value, divide the annual cash distribution by 85%, advises Bowler. Take

IDS/Shurgard Growth II, a 1989 miniwarehouse deal sold for \$250 per unit. It currently pays out \$16.25 a year in cash distributions. Divided by 0.085, each unit would be worth about \$190. Indeed, one unit recently traded in the secondary market at \$195. Discounts to net asset

value are steeper for partnerships with higher debt and lower payouts.

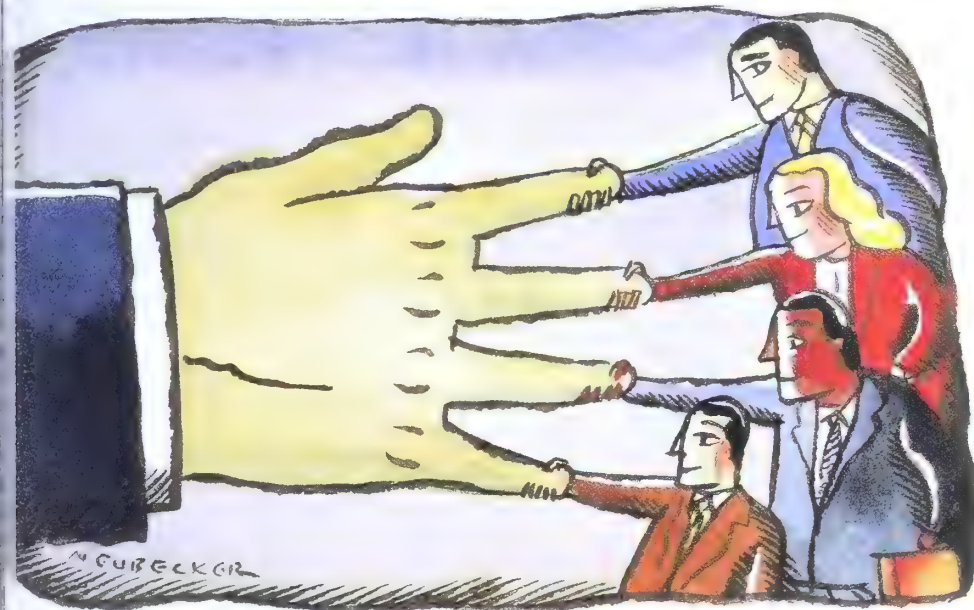
There are other considerations when buying partnerships besides valuation, however. Most important is the general partner, or sponsor. Many of them have gotten a bad rep—for good reason.

ing assets. Details should be reported in the most recent 8-K. Unit prices will probably be bid up, but the risk is minimized because the investment time is capped. Avoid deals where the liquidation time tops three years, and try to discern how long your money will be tied up before you buy.

You'll also want to take a look at the cash-distribution histories. Several partnerships are highly leveraged and stopped cash payouts during the real estate recession. It's best to buy into deals that have had consistent cash distributions. Also, check financial statements to make sure cash flow from rents and other sources is enough to cover payouts. Balcor Colonial Storage, an unleveraged miniwarehouse deal sold in 1986 at \$250 per unit, paid quarterly distributions until it was liquidated for \$256 per unit late last month. In general, expect 8% to 11% yields on units of unleveraged real estate deals.

AND LOCATION. Of course, the type of real estate makes a difference. Miniwarehouses and apartments are hot. Attractive deals to consider, suggests Bowler, are IDS/Shurgard series, Balcor Realty 85-2, and Dean Witter Coldwell Banker Tax Exempt Mortgage Portfolio. But many older office buildings have become obsolete, and their values probably won't rebound. So before buying into any office deal, look closely at vacancy rates, the location of the properties, the number of leases coming up for renewal, and lease provisions. You'll also want to consider the fee you'll pay your accountant at tax time: Limited partnerships are notorious for creating tax-preparation headaches.

Still interested? Although limited partnerships are often very complex, their returns can be quite rewarding. So happy hunting—but remember: Understand exactly what you're buying, or don't bother. *Toddi Gutner*



And Where to Sell Partnerships

Here are some firms that make a secondary market in publicly registered limited partnerships or that sell units on commission. Ask about fees, commissions, and length of time for transactions to clear.

FIRM	PHONE NUMBER
CAN PARTNERSHIP SERVICES	800 736-9797
DW MANAGEMENT	800 431-7811
GO PARTNERSHIP BOARD	800 272-6273
R & ASSOCIATES	800 274-9991
Y RESOURCES GROUP	617 876-4800
YLINE SECURITIES	800 355-9757
ASSET MANAGEMENT	800 654-6110
ENZIE PATTERSON SECURITIES	800 854-8357
NAL PARTNERSHIP EXCHANGE	813 222-0555
NWIDE PARTNERSHIP MARKETPLACE	800 969-8996
IC PARTNERSHIP GROUP	800 727-7244
ERSHIP SERVICE NETWORK	800 483-0776
IND JAMES & ASSOCIATES	800 248-8863
ID MARKET CAPITAL SERVICES	800 999-7793
IDARY INCOME FUNDS	708 325-4445
ITIES SERVICE NETWORK	407 496-5387

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Several general partners, such as now-bankrupt Integrated Resources and Southmark, put their fee-raking motives before the interests of their limited partnerships. "The general partners have complete control," says Matt Rigg, a Miami financial planner who invests in limited partnerships. So stick with partnerships that have high-quality, well-known management and good track records. The prospectus should report prior results. Also, look for deals where sponsors sold partnerships to their own clients, as in the case with brokerage firms and insurance companies such as Merrill Lynch and CIGNA.

HOW LONG? Those with less stomach for risk may want to invest in partnerships that are liquidating or have announced the intention to do so. PaineWebber, Dean Witter, JMB Realty, Merrill Lynch, and Balcor, which is owned by American Express, are all in the process of sell-

TURBOCHARGED BONDS —SO BETTER BUCKLE UP

Callable step-up bonds may not be a household name, but the companies and government agencies that issue them are. General Electric, Xerox, and Fannie Mae are but a few recent issuers.

These fancy-sounding products are the most popular form of what Wall Street calls structured notes, which are bonds loaded with bells and whistles. Callable step-ups are high-quality bonds with an above-market interest rate, a call feature, and a coupon that increases annually over the life of the bond. It's because the bonds are complex that they promise higher interest rates—and more risk—than simpler, noncallable securities.

RATE VICTIMS. Sounds enticing, especially for investors looking to lock in some profits from the overheated stock market and get some fixed-income exposure. Indeed, the bonds are once again gaining in popularity after an industry shakeout in 1994. At that time, these bonds were structured much more aggressively. While they were designed to perform extremely well when interest rates were low, they had a dramatic downside when interest rates rose. Some were set up so that if interest rates increased past a certain point, bondholders would get no return at all. Of course, interest rates surged in 1994, and these bonds lost their appeal. Today, callable step-up bonds, which are actually derivatives sold by stockbrokers in denominations as little as \$1,000, are designed to be much more balanced across varied interest-rate environ-

ments, so demand is picking up. The \$2.2 billion in callable step-up notes issued so far this year is more than the \$2.1 billion issued in all of 1995, according to Securities Data.

Still, like most Wall Street-engineered products, there are hidden risks which often make these fixed-income instruments a bad buy—espe-

cially if you must have access to your principal at a set time in the future. First, it is important to understand how callable step-up coupon notes work. Take, for example, a recent Freddie Mac issue, sold at par with a 10-year final maturity in 2006 and initial interest rate of 7%. It is callable after one year and any time beyond that with 10 days' notice. If Freddie Mac decides to call the bond after a year, then the investor will have earned a 7% return, vs. the 5.58% yield on a one-year Treasury bought at the time of Freddie Mac's issue. If Freddie Mac chooses not to call the bond, then the yield increases to

7.10% in 1997 and rises incrementally each year, until it reaches 9% the last year before maturity. If the bond is held until maturity, it will

are called after the first year. It makes sense: If the coupon is going to increase more than the interest rate, it's best for the issuer to call the bond. So it's unlikely the investor ever will reap the highest advertised yields.

But that's only half the story. If interest rates rise sharply, what was sold as a one-year bond could easily be held until final maturity, be 5, 10, or 15 years. And with any long-term fixed-income product, the risk of rising interest rates means potential for capital loss.

INEFFICIENT MARKET.

the big problem with these securities is that they force buyers to commit to the investment for a specific term while the issuer has the option to back out at any time. That leaves investors without any way to fully analyze the risk of complex call options. While it's possible to sell the bonds before they are called, investors will more than likely lose money, since they would probably get less than par for them. That's partly because these bonds trade in a relatively inefficient market.

What's more, during periods of declining interest rates, callable bonds won't appreciate in value as much as noncallable notes because potential buyers fear the bonds will be called, and nobody will pay a premium for them, says Sanford Bragg, managing director of Standard & Poor's management ratings department. The result: minimal price appreciation.

So, if there's even the slightest chance you'll need your investment anytime soon, skip the seductive sales pitch and the promise of higher yields for noncallable. Keep it simple, and buy Treasury security or short-term bond fund to park your cash or profits from the stock market.

Todd Guttm

Callable Step-Up Coupon Notes

These hotly marketed instruments promise top rates. But higher yields may not compensate for the increased risk.

ADVANTAGES

- ▶ Offers higher interest rate than is currently available in the Treasury market.
- ▶ Coupon increases, or steps up, each year for the life of the bond.
- ▶ High-quality issuers such as Fannie Mae, General Electric, and Xerox.
- ▶ Most liquid of all structured notes.

DISADVANTAGES

- ▶ Timing of principal payment is unknown. In general, the bonds will be called unless interest rates rise significantly.
- ▶ Investor needs to reinvest funds—often at lower rates—if the bonds are called.
- ▶ Minimal price appreciation compared to noncallable notes.

cially if you must have access to your principal at a set time in the future.

First, it is important to understand how callable step-up coupon notes work. Take, for example, a recent Freddie Mac issue, sold at par with a 10-year final maturity in

give an average yield that is approximately 100 basis points above that of a 10-year Treasury note. Noncallable 10-year Freddie Mac paper currently yields only 30 basis points more than Treasuries.

The trickiest part of these bonds is the call option. Investors often are sold callable step-up notes as short-term fixed-income products with the assumption that they will be retired after the first year. The sales pitch compares the first-year yield with that of a one-year Treasury. In general, when interest rates are stable or falling, these bonds

Since these bonds can be called, the investor may never see the high yields that were hyped



SAY "GLUG": BW's Lowry Miller, shot with a Nikonos V

We opted instead for the Nikonos V, by Nikon. It's pricier, at \$1,036 for just the body and a 35mm lens. But it's easy enough to handle for amateurs while taking professional-quality photos, and it can easily be serviced worldwide. You'll need a strobe as well. The \$820 Nikonos SB-105 strobe has some nifty features once reserved for more professional models, such as more

flash power, a faster recycle time, and a repeating-signal flash for emergencies. An alternative is the Ikalite family of strobes, ranging from \$300 to \$950. They're good quality and compatible with Nikonos.

If you settle on the Nikonos, call your nearest PADI International dive center and order their manual, *Underwater Photography: Camera Basics and Equipment Care* (\$13.50). It explains far more clearly how to use and care for the Nikonos V than the owner's manual.

Then, be sure to invest in a few lessons. Many resorts and live-aboard cruises offer

photographer. He offers a handy two-day course to cover the basics for \$100 a day, including tanks and boat dives, but he can arrange a longer, more detailed program as well.

Peter started us off slowly, with shallow dives in a protected bay so we could get accustomed to handling the equipment. Classic mistakes riddled our first couple of rolls: a nice collection of fish tails, dots from the flash reflecting on stirred-up sand, too much rocky background from shooting down instead of out into the blue. In the evening over beers, we'd go over each frame as he critiqued our judgment of distance, composition, and subject matter. Most important, he showed us how to maintain the camera. Properly greasing the O-rings that seal each opening is crucial. If the camera floods, as we thought ours had for a few panic-stricken hours after the third roll of film, you may as well just toss the whole thing out unless you can get it to a professional dealer fast.

REEF FEVER. It can be so much fun floating upside down to peer into holes that you forget the most basic lesson: Diving comes first, and you must remain alert no matter what distraction. But by the time we concluded our second week as photographers, we could navigate caves, stalk their beautiful denizens, and sneak up on poisonous lionfish with ease.

Taking up underwater photography has made both of us better divers. Hovering six inches above a reef without destroying 200 years' worth of coral growth does wonders for your skills. Plus, each dive is more vivid,

because your eye is trained to notice much more than before. Best of all, the results help give your family and friends an inkling of why you're so hooked on the sport. *Karen Lowry Miller*

TO THE DEEP— WITH LENS AND STROBE

Whether it is the thrill of spying on an alien universe, the light in spotting an elusive manta ray, or simply the joy of being underwater, diving is never dull. But if you've thought of taking past

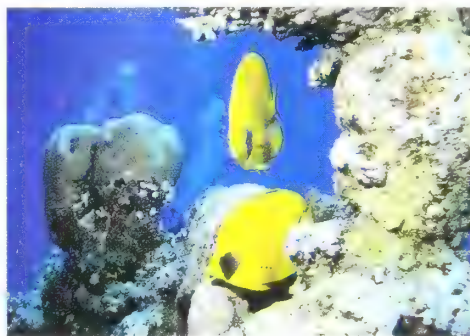
PHOTOGRAPHY

your reef wall is starting to make you feel restless, you won't have to taunt great whites from a cage to add a challenge to your sport. Instead, taking up underwater photography may do the trick. Camera experience is even required. In fact, it helps not to have to break bad habits to fit underwater conditions. Nor must you first complete hundreds of dives—my band, Scott, and I had been diving for only three years when we treated ourselves to an underwater camera for our Red Sea trip in 1977. All you need is good buoyancy control—the ability to hover in one place—and feel comfortable enough to rig your gear to free up a hand for the camera. Before handing over your

credit card, however, talk to experts at a good dive or photo shop and read the photo columns in dive magazines to find what's right for you. One option is to purchase a waterproof housing for an SLR land camera—running \$600 to \$2830, depending on the model of your camera.

It allows you to look directly through the lens rather than a viewfinder. But it struck us as complicated, and bulky, and we don't own a decent camera anyway.

CUMBERSOME. At the other extreme is the Motormarine 35, made by Sea & Sea U/W Photography, a fixed-flash unit with a single 32mm lens that's good for basic snapshots. Sea & Sea also makes a MotorMarine 2EX, with a detachable strobe and lenses that can be changed underwater, for about \$1120, strobe included. But we couldn't imagine having time to switch from a macro to a wide-angle lens if a hammerhead swims by.



RED SEA: Photo lessons are a big help

weeklong lessons. We dove with Oonadivers, a top-notch outfit in Sharm el Sheikh at the southern tip of Egypt's Sinai peninsula. One of their divemasters is Peter Dalton, an award-winning British

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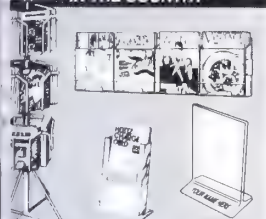
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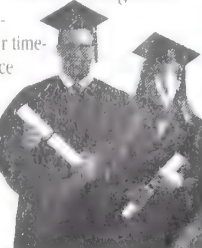
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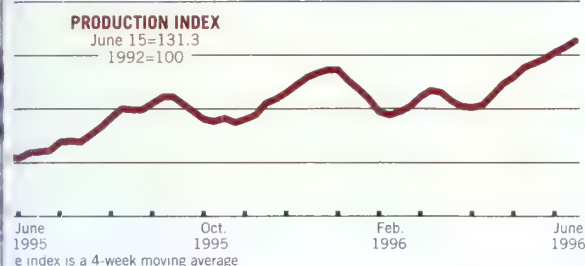
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PRODUCTION INDEX

Change from last week: 0.5%
Change from last year: 8.5%



The production index increased moderately during the week ended June 15. However, before calculation of the four-week moving average, the index had declined to 131.6, from 131.9. In the latest week, declines in the seasonally adjusted output levels of autos, trucks, and steel, as well as in rail-freight traffic, offset production gains in coal, lumber, paper, and electric power. The leading index will be unavailable for an indefinite period of time.

Production index copyright 1996 by The McGraw-Hill Companies

TRADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (6/21) S&P 500	666.84	665.85	21.9
CORPORATE BOND YIELD, Aaa (6/21)	7.90%	7.93%	6.8
INDUSTRIAL MATERIALS PRICES (6/21)	106.0	106.9	-7.4
BUSINESS FAILURES (6/14)	NA	NA	NA
REAL ESTATE LOANS (6/12) billions	\$507.8	\$506.1r	4.9
KEY SUPPLY, M2 (6/10) billions	NA	NA	NA
FINANCIAL CLAIMS, UNEMPLOYMENT (6/8) thous.	361	354	-4.2

Sources: Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
MUTUAL FUNDS (6/25)	5.15%	5.27%	5.95%
COMMERCIAL PAPER (6/25) 3-month	5.50	5.50	5.94
CERTIFICATES OF DEPOSIT (6/26) 3-month	5.48	5.46	5.91
FIXED MORTGAGE (6/21) 30-year	8.50	8.57	7.74
ADJUSTABLE MORTGAGE (6/21) one-year	6.08	6.15	5.84
RENTAL RATE (6/26)	8.25	8.25	9.00

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

All data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

PERSONAL INCOME

Monday, July 1, 8:30 a.m. EDT ▶ Personal income likely grew 0.5% in May, the same as in April, says the median forecast of economists surveyed by MMS International of The McGraw-Hill Companies. Consumer spending likely rose 0.6% in May after a 0.1% increase in April.

CONSTRUCTION SPENDING

Monday, July 1, 10 a.m. EDT ▶ Building output was probably flat in May, after increasing 1.4% in April.

PM SURVEY

Monday, July 1, 10 a.m. EDT ▶ The National Association of Purchasing Management's

business index likely edged up to 51% in June, from May's 49.3%.

LEADING INDICATORS

Tuesday, July 2, 8:30 a.m. EDT ▶ The Conference Board's index of leading indicators probably rose 0.2% in May.

NEW HOME SALES

Tuesday, July 2, 10 a.m. EDT ▶ New homes likely sold at a 740,000 annual rate in May, after jumping 6.7% in April, to 776,000.

FOMC MEETING

Tuesday, July 2 ▶ Policymakers at the Federal Reserve Board will meet to set monetary policy for the next six weeks. Econo-

mists expect no change in short-term interest rates. The meeting ends July 3.

FACTORY INVENTORIES

Wednesday, July 3, 10 a.m. EDT ▶ Manufacturing inventories probably grew by 0.3% in May, after no change in April. That's suggested by the solid gain in factory production in May.

EMPLOYMENT

Friday, July 5, 8:30 a.m. EDT ▶ The MMS median forecast calls for a healthy addition of 150,000 jobs to June nonfarm payrolls, on top of the 348,000 jobs created in May. The June unemployment rate is expected to remain at May's low 5.6%.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (6/22) thous. of net tons	1,983	2,051#	1.6
AUTOS (6/22) units	139,418	142,178r#	11.6
TRUCKS (6/22) units	119,427	123,349r#	-4.0
ELECTRIC POWER (6/22) millions of kilowatt-hrs.	70,688	66,360#	4.8
CRUDE-OIL REFINING (6/22) thous. of bbl./day	14,250	14,252#	-3.3
COAL (6/15) thous. of net tons	20,189#	19,828	9.1
PAPERBOARD (6/15) thous. of tons	878.9#	886.0	7.4
PAPER (6/15) thous. of tons	815.0#	816.0r	-1.2
LUMBER (6/15) millions of ft.	480.8#	469.0	8.3
RAIL FREIGHT (6/15) billions of ton-miles	25.5#	25.5	4.9

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPAl, SFPa2, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (6/26) \$/troy oz.	383.800	386.300	-1.4
STEEL SCRAP (6/25) #1 heavy, \$/ton	138.50	136.50	-1.4
COPPER (6/22) ¢/lb.	105.1	112.5	-27.9
ALUMINUM (6/22) ¢/lb.	69.8	70.3	-18.2
COTTON (6/22) strict low middling 1-1/16 in., ¢/lb.	79.88	81.67	25.1
OIL (6/25) \$/bbl.	19.88	21.26	11.1

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (6/26)	109.55	107.97	84.79
GERMAN MARK (6/26)	1.53	1.52	1.38
BRITISH POUND (6/26)	1.54	1.54	1.59
FRENCH FRANC (6/26)	5.17	5.16	4.86
ITALIAN LIRA (6/26)	1534.9	1535.2	1640.0
CANADIAN DOLLAR (6/26)	1.36	1.37	1.38
MEXICAN PESO (6/26)*	7.603	7.522	6.270

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

This Week, Online

Business Week presents frequent live conferences on America Online. It's your opportunity to ask questions about features from the magazine.

Sunday

Halfway through 1996, the economy is steaming along at a surprisingly fast clip. Kathleen Madigan, of BW's influential Business Outlook column, takes questions—and shares her insights—on what's in store for the rest of the year and beyond.

June 30

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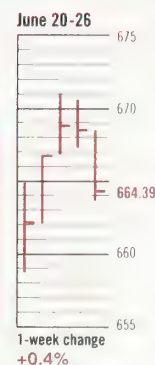
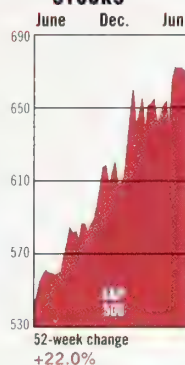
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Investment Figures of the Week

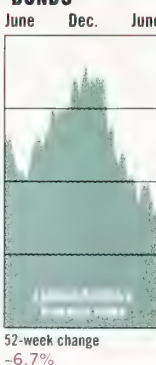
MENTARY

ing demand for Treasuries ed up the bond market, and -term interest rates eased, ing back down toward 7%. helped the blue-chip stocks in some lost ground. Even with 26's drop of 37 points in the the average finished in the column for the week. But the the-counter market continued ll off, especially tech issues. lasdaq Composite Index ed another 2.2%. Since hit- its high three weeks ago, lasdaq index has lost 7.7% value.

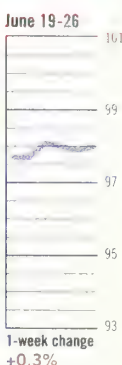
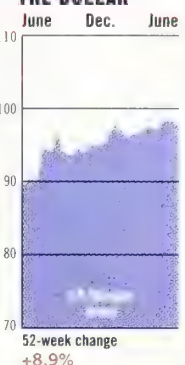
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change	
		Week	52-week
JONES INDUSTRIALS	5682.7	0.6	24.7
DOW JONES INDUSTRIALS (S&P MidCap Index)	231.2	-2.3	17.9
DOW JONES INDUSTRIALS (Russell 2000)	339.8	-2.1	21.4
DOW JONES INDUSTRIALS (Russell 3000)	378.0	-0.2	22.1
FOREIGN STOCKS	Latest	% change (local currency)	
		Week	52-week
DOW JONES INDUSTRIALS (FINANCIAL TIMES 100)	3695.5	-1.5	12.6
DOW JONES INDUSTRIALS (NIKKEI INDEX)	22,666.8	1.3	55.1
DOW JONES INDUSTRIALS (TSE COMPOSITE)	5027.7	-0.9	11.0

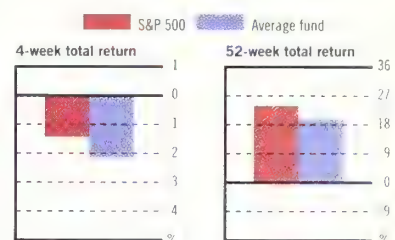
FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.22%	5.23%	5.55%
30-YEAR TREASURY BOND YIELD	7.04%	7.11%	6.51%
S&P 500 DIVIDEND YIELD	2.15%	2.16%	2.45%
S&P 500 PRICE/EARNINGS RATIO	19.1	19.1	16.8
TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	627.3	625.0	Positive
Stocks above 200-day moving average	59.0%	59.0%	Neutral
Speculative sentiment: Put/call ratio	0.68	0.72	Neutral
Insider sentiment: Vickers sell/buy ratio	2.49	2.31	Neutral

INDUSTRY GROUPS

MONTH LEADERS		% change		Strongest stock in group	% change		Price
		1-month	12-month		1-month	12-month	
MANUFACTURED HOUSING		8.3	49.3	FLEETWOOD ENTERPRISES	8.3	51.5	30 ⁷ / ₈
PHOTOGRAPHY/IMAGING		4.0	26.2	POLAROID	4.2	7.6	46 ¹ / ₈
OIL EXPLORATION AND PRODUCTION		3.8	14.2	BURLINGTON RESOURCES	10.1	13.1	42 ¹ / ₈
SPECIALTY RETAILERS		3.8	26.1	CIRCUIT CITY STORES	14.3	12.5	36
HOUSEHOLD PRODUCTS		3.4	27.7	COLGATE-PALMOLIVE	6.5	14.4	85 ⁵ / ₈
MONTH LAGGARDS		% change		Weakest stock in group	% change		Price
		1-month	12-month		1-month	12-month	
OLD MINING		-10.9	5.1	ECHO BAY MINES	-12.6	16.1	11 ¹ / ₄
IRONWORKS AND APPLIANCES		-10.5	3.2	WHIRLPOOL	-14.5	-10.8	48 ³ / ₄
COMPUTER SYSTEMS		-9.5	8.4	APPLE COMPUTER	-22.9	-57.7	20 ⁵ / ₈
PACKAGING		-8.9	-13.6	CALIBER SYSTEM	-10.7	-17.4	34 ³ / ₈
OIL AND GAS DRILLING		-8.9	53.3	ROWAN	-9.9	91.9	14 ¹ / ₈

MUTUAL FUNDS

LEADERS	4-week total return	%	LAGGARDS	4-week total return	%
INTOBER EASTERN EUROPEAN EQUITY	7.1		STEADMAN TECHNOLOGY GROWTH	-17.4	
ARBURG PINCUS ADVISOR JAPAN GROWTH	4.3		PREMIER STRATEGIC GROWTH	-15.8	
TRADITIONAL GREATER INDIA	4.2		WASATCH MID-CAP	-14.2	
LEADERS	52-week total return	%	LAGGARDS	52-week total return	%
NDMARK SMALL CAP EQUITY A	96.8		STEADMAN TECHNOLOGY GROWTH	-30.6	
RNER SMALL CAP EQUITY	67.2		STEADMAN AMERICAN INDUSTRY	-20.0	
ANKLIN GLOBAL HEALTH CARE	64.8		STEADMAN INVESTMENT	-17.3	



RELATIVE PORTFOLIOS

Amounts represent the net value of \$10,000 invested one year ago in each portfolio.

Percentages indicate daily total returns.



U.S. stocks
\$12,562
+0.97%



Foreign stocks
\$11,826
-0.31%



Money market fund
\$10,534
+0.11%



Gold
\$10,272
+0.26%



Treasury bonds
\$9,931
+0.51%

Data on this page are as of market close Wednesday, June 26, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as

of market close June 25. Mutual fund returns are as of June 21. Relative portfolios are valued as of June 25. A more detailed explanation of this page is available on request. r=revised

A PLAN TO BOOST ECONOMIC GROWTH

In this political season, there is one overriding question: Can the U.S. economy grow faster? The answers are "yes," "no," "kinda," "maybe," and "why should it?"

To cut through the clutter and the confusion, *BUSINESS WEEK* offers up its own proposal. We think the economy can grow a full percentage point faster every year: 3% instead of the current 2% long-term rate. Over time, an increase of just one point would have an enormous impact on wages, job creation, and profits. We believe we have a sensible, pragmatic program to get us there—one that doesn't take the wild risks of a radical flat tax or repeat the mistakes of another big supply-side tax cut (been there, done that, and still paying interest on it). The *BUSINESS WEEK* plan attacks the core problem of America's anemic growth: too little savings and too little investment. It is a realistic plan to expand the wealth of this nation (page 90).

But first let's dispel a few myths. No. 1 is that with gross domestic product expected to come in above 4% in the second quarter, there isn't any growth problem. We beg to differ. Despite the second-quarter pop, economic growth has still averaged only 1.7% in the past year, and over the past six years, it has averaged a measly 1.9%. Myth No. 2 is that with capital spending running at double-digit rates for two years, there isn't a savings and investment problem either. Again, we think otherwise. Net national savings average only 5% of output, down from 11% during the hot-growth 1960s. And despite heavy spending on computers, net equipment investment is crawling along at only 2% of GDP.

So let's not kid ourselves. We've got real problems. Here are major solutions. They're not particularly trendy, but they are sound enough to boost growth to 3% without renewed inflation.

Begin by ending Washington's drain on savings by finally balancing the budget. The Republicans and Democrats are close. A budget that curbs entitlement spending and glides toward balance in seven years will lower long-term rates and the cost of capital by nearly two percentage points. Go for it.

Next, clean up the tax code and roll back marginal rates. This doesn't require a new tax system, just a return to the Tax Reform Act of 1986. Closing loopholes and shelters could fund sharp cuts in tax rates. They could drop back to the early brackets of 15% and 28%, from the present top rate of about 40%.

Privatizing Social Security is the most dramatic part of the *BUSINESS WEEK* plan. By converting Social Security to a fully funded pension system, the U.S. can boost its savings. This is how privatization would work: Social Security would be broken into three parts, each supported by a portion of the existing 12.4% payroll tax. A standard pension for workers would be supported by a 5% payroll tax. Survivors' and disability insurance would be financed by a 2.4% payroll tax. And new Personal Security Accounts would be funded by a 5% tax. PSAs are in effect, like 401(k) defined-contribution accounts, where individuals would invest in stocks, bonds, or other investments that receive substantially higher real rates of return than the 2% Social Security funds earn.

What's the downside to the *BUSINESS WEEK* plan? By investing a portion of their Social Security themselves, people must accept a higher level of risk. And paying for the transition to a privatized Social Security will be costly. Getting an extra 1% growth may not sound like much, but it would make all the difference in the world. It means more income and a better retirement for nearly everyone. It means the end of economic anxiety.

TIME FOR CONGRESS TO GET CRACKING

Let's give the 104th Congress its due. It helped change the terms of political debate in America, making balancing the budget a serious issue (albeit a fading one in this Presidential election season as candidates rush to cut taxes and pander for votes). The 104th also began to apply the laws of the land to Congress, which is belated progress of sorts. And it passed two important bills—lobby reform and farm subsidy reform.

But this is pretty meager fare given the great promise of the 104th when it was voted into office in 1994. The actual legislative accomplishment to date is below par, and time is running out. There are only a few working weeks left for Congress to do the serious work the nation expects of it. We hope the new Senate Majority Leader Trent Lott (R-Miss.) and Senate Minority Leader Thomas A. Daschle (D-S.D.) can hold their respective extremists at bay to make the compromises necessary to get things done.

Take the health-care reform bill. The two sides agree on the Kennedy-Kassebaum, which would provide health-

insurance portability and exempt preexisting conditions. The only dispute is about Medical Savings Accounts, an intriguing new concept that can wait until next time. Sacrificing important health-care reform for MSA is an outrage.

Ditto for welfare reform. There is consensus on getting people to work for their benefits and placing time limits on receiving them. This is breakthrough stuff. But hardline conservative legislators insist on ending Medicaid entitlement for poor people. We say drop that proposal and pass the bill. Neither this Congress nor this Administration has done much to end middle-class entitlements or special benefits to corporations this year. So let's give the poor a break.

Our wish list for legislation extends to campaign finance reform (killed by the Senate, but beloved by most Americans) and reform of the Food & Drug Administration and the Federal Aviation Administration. The 104th Congress still has a chance to make its mark in history. It should seize the day.



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"What those guys did was great."

—Akira Isahai,
Project Manager,
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"We always have to contend with a PC marketplace that changes at a very rapid pace. And as NEC Technologies has grown into a \$2.4 billion company, we developed some natural complications that were slowing us down a little. Our legacy systems weren't flexible enough to support the speed of change. And we had several piecemeal systems that didn't talk very well to one another.

"Order information took too long to get to manufacturing and distribution, creating problems for our supply chain of distributors, retailers and corporate end-users. Our delivery dates weren't as accurate as we wanted. And it was difficult to react quickly to the configuration preferences indicated by the marketplace.

"SAP software was the answer. Specifically, the modules for financials, controlling, materials management, production planning, sales and distribution and human resources. And needless to say, we didn't want to waste any time getting them installed.

"So we assembled a team of high-level users at NEC to work with our consultants. Our people weren't technically oriented, but did have a deep understanding of our business. We knew they could make good business decisions about our processes and then apply them to configuring the SAP software.

"Thanks in no small part to our rather novel approach, we had 1,400 users up and running in only eight months.

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INSIDE MICROSOFT

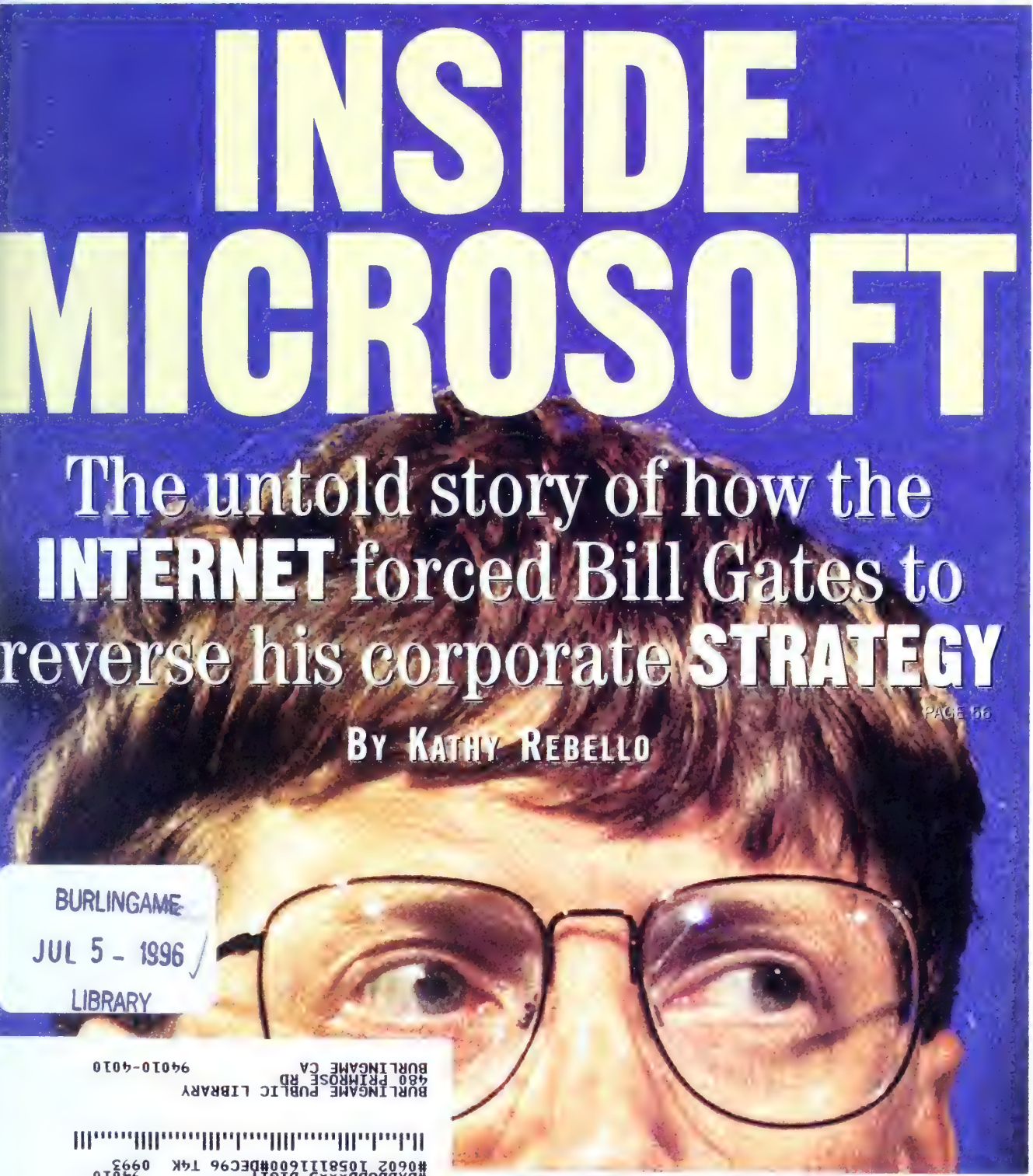
The untold story of how the **INTERNET** forced Bill Gates to reverse his corporate **STRATEGY**

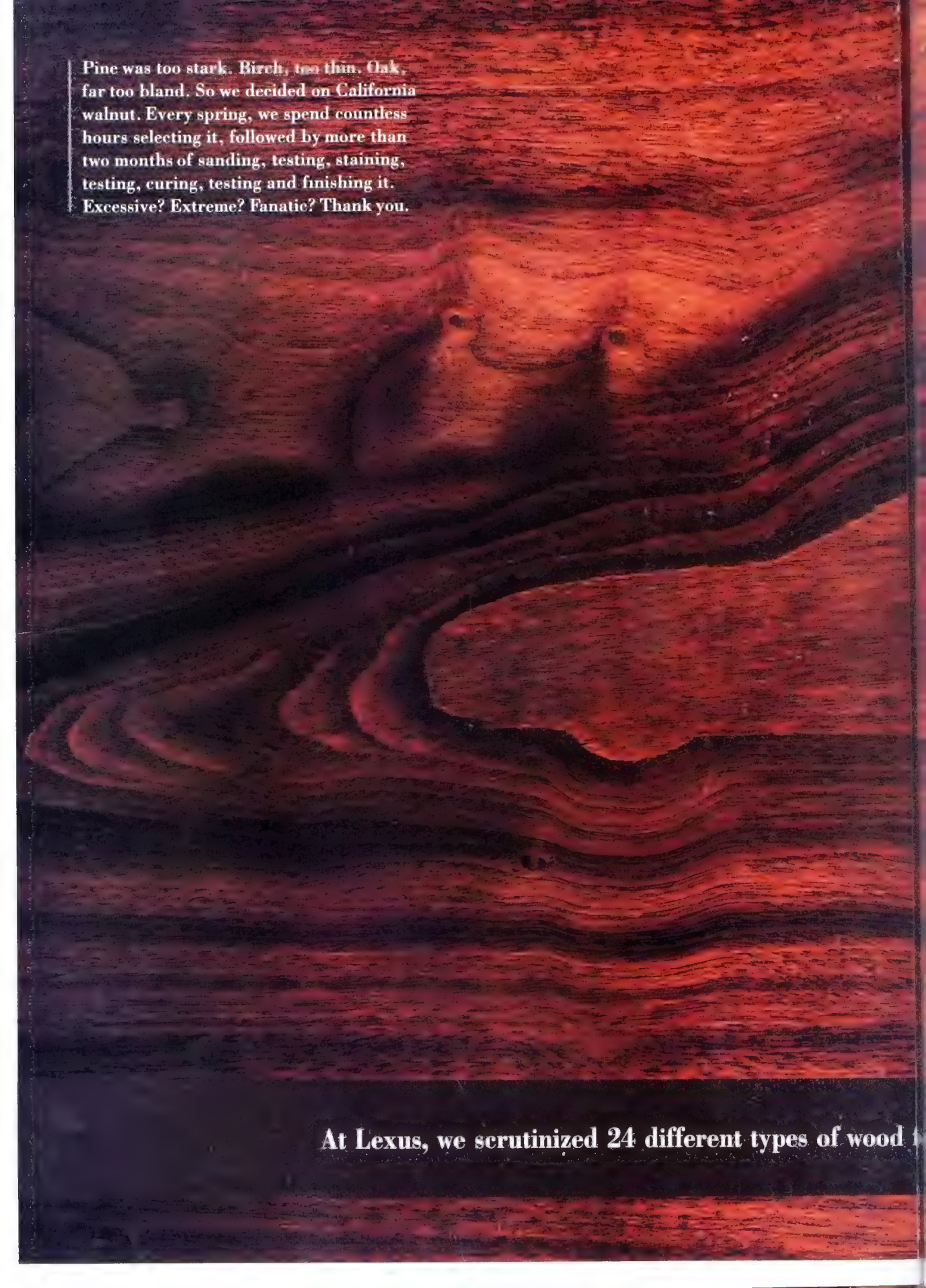
BY KATHY REBELLO

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Pine was too stark. Birch, too thin. Oak, far too bland. So we decided on California walnut. Every spring, we spend countless hours selecting it, followed by more than two months of sanding, testing, staining, testing, curing, testing and finishing it. Excessive? Extreme? Fanatic? Thank you.

At Lexus, we scrutinized 24 different types of wood.



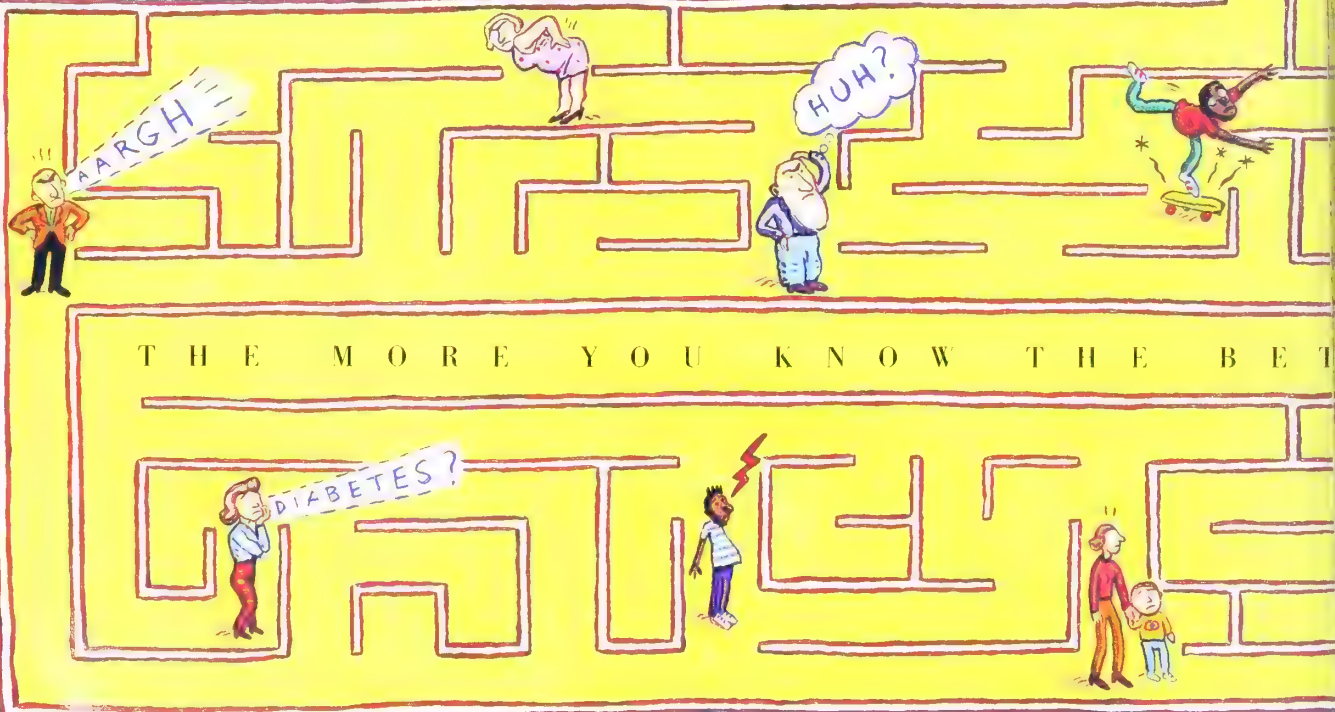
interior before we found one that made the cut.

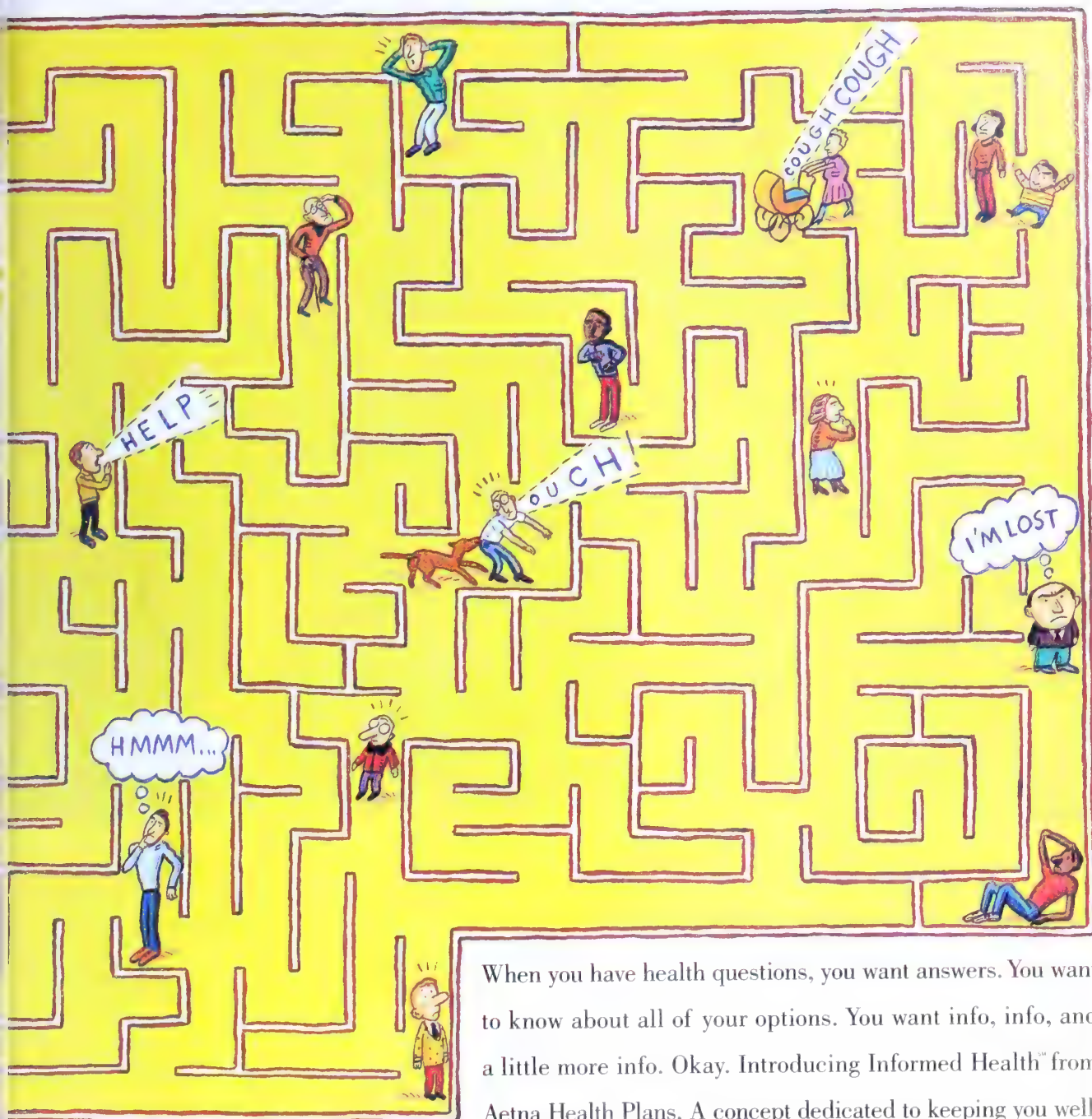
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___ the ___ information, ___ care ___ so ___.

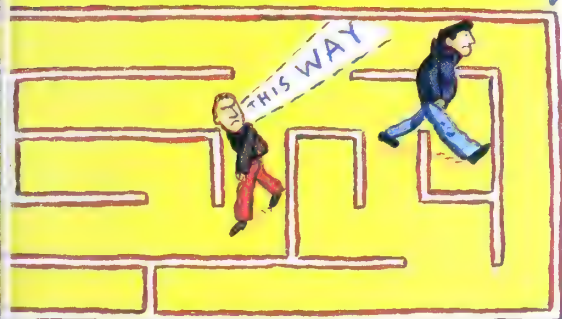
With ___ right information, ___ isn't ___ puzzling.

With the right information, health care isn't so puzzling.





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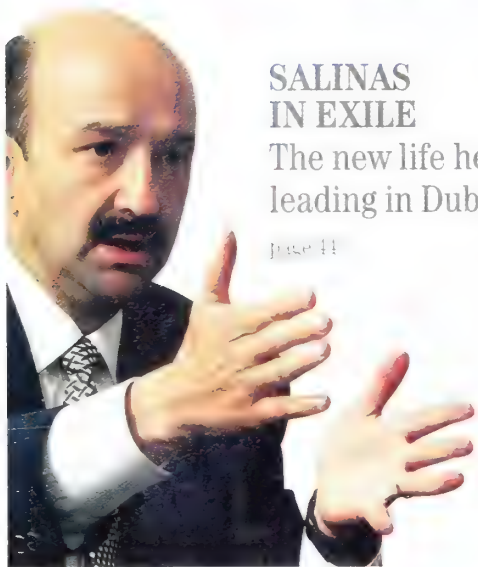
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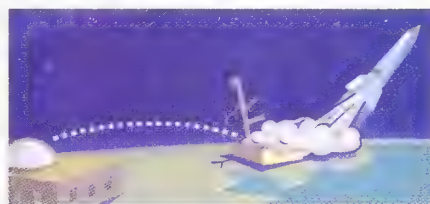


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Up Front

EDITED BY LARRY LIGHT

THE FEDS

WILL SHE CALL IT FEAR OF FLYING II?

MARY SCHIAVO, WHO IS THE Transportation Dept.'s chief in-house critic of the FAA, might quit to write an insider's book, say well-placed figures in publishing.

They say that her agent, Suzanne Gluck of ICM, is shopping a book that publishing people expect to go into the serious safety critiques she has been leveling at the Federal Aviation Administration. Schiavo, 40, Transportation's inspector general since 1990, could resign her \$115,700-per-year job if publishers show enough interest, they say. There's no evidence Schiavo is being forced out.

Before sending out the proposal, Schiavo's agent has



SCHIAVO May step down

insisted would-be publishers sign a confidentiality agreement not to discuss the book, say the sources. Schiavo and Gluck didn't return phone calls. Publishing insider Richard Frishman, president of publicity firm Planned Television Arts, speculates that Schiavo could land an advance of \$300,000 and perhaps far more. *Willy Stern*

CONSUMER BEWARE

GRIPE ALL YOU WANT, BUT IT'LL COST YOU

FOR NEARLY 80 YEARS, THE Better Business Bureau has fielded consumer phone calls gratis. Probably not for much longer. The nation's 137 bureaus now are voting on a plan, expected to pass, to charge you for checking out your plumber or complaining about the job he did.

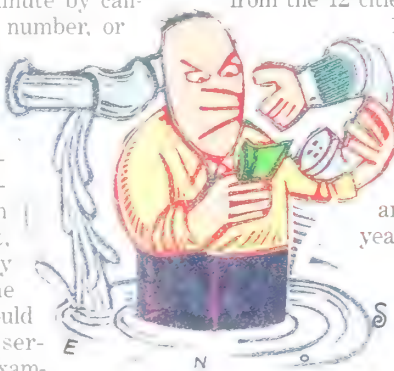
How much? In a three-year nationwide test the bureaus ran, consumers paid 95¢ per minute by calling a 900 number, or a \$3.80 flat rate using a credit card. Individual bureaus can opt out, but likely won't. The money would expand service, for exam-

ple, by hiring more operators to avoid busy signals.

But Consumer Federation's Stephen Brobeck says customers may be hurt where the bureau is the only help around. St. Louis BBB Vice-President Michelle Corey, a fee foe, thinks poorer people simply won't call.

Statistics are murky on this point. The bureaus have not released results from the 12 cities tested from 1993 to 1995. Yet nationwide, calls fell 28% in 1994, to 10.6 million. (No results are in for last year.) Proponents contend that calls were miscounted.

Randi Feigenbaum



TALK SHOW "We have been under restrictions for 40 years already, and it's time to move on."

—IBM's general counsel, Lawrence Ricciardi, on an agreement with the feds to end the last terms of a 1956 antitrust decree

I-WAY PATROL

MSNBC: FIRST, GET THE ADDRESS RIGHT

FOR WANT OF \$100, MSNBC nearly lost its Internet address. On Dec. 15, the day after Microsoft and NBC announced they would spend hundreds of millions to launch a cable news channel and Web site called MSNBC (page 68), Van Nuys (Calif.)-based Micro Solutions Network Boards Corp. claimed for itself the Internet address of www.msnnbc.com.

The Microsoft-NBC MSNBC channel didn't discover the potential fiasco until this spring, when it tried to register its Internet address with Network Solutions Inc., which administers these things. Micro Solutions, which couldn't be reached for comment, gave up its coveted address and got in return Microsoft software worth thousands.

Then came more trouble. Turns out that Micro Solutions had never paid NSI its \$100

registration fee. Since the Microsoft-NBC MSNBC took months to notify NSI it had taken over the address, NSI dunning notices on the default account were sent astray. MSNBC finally paid its bill on June 13, but NSI erred and pulled the plug on msnnbc.com anyway on July 25. The mess g-



fixed the next day, and the site is up and running again.

"There were errors on both sides," says an NSI spokeswoman. If its luck holds, MSNBC launches on July 15. *Elizabeth Lesch*

HONCHOS

'I DUB THEE SIR ALEX OF MOTOWN'

FORD'S CHAIRMAN has a new title: Sir Alex. Queen Elizabeth II has selected British-born Alex Trotman as a Knight Bachelor. Soon (date yet unscheduled), the executive will march into the Royal Ballroom at Buckingham Palace and go down on one

knee before the Queen. As in days of old, she will touch him on each shoulder with her sword and declare: "Arise, Sir Alex."

The Palace says the award is for his "contributions to Anglo-American commercial relations." Ford is the top-



TROTMAN: On Her Majesty's list

selling auto brand in Britain, employing 40,000 there. Trotman, who perhaps now will be squired around in a Ford Crown Victoria, is the first

Detroit chieftain to get a knighthood—an honor only a Brit can receive (he has dual citizenship). Among the few U.S. corporate kingpins to be knighted is Dennis Weatherstone. The retired J.P. Morgan chairman even has a Motor City connection. He's on GM's board.

Trotman is one of 1,041 commoners the Queen is elevating in her Birthday Honours List. Ford execs claim Trotman is not demanding much deference from his serfs. Says one veep: "We still call him Alex around the office." *Keith Naughton*

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TRENDETS

THE YOUNG AND THE CLUELESS

INVESTMENT SEMINARS ARE everywhere in the workplace these days. A recent William M. Mercer study shows that 75% of companies offer investment education, up from just 44% in 1993. Trouble is, it isn't working, at least among the people who need educating the most.

The seminars are targeting employees who haven't signed up for 401(k)s and other retirement plans. But the non-savers, particularly younger ones, aren't coming. That leaves some seminars preaching to the converted: older and better-off employees.



Tektronix, a technical-equipment company in Beaverton, Ore., invited non-saving employees by name, offering each \$6 as an incentive. Yet less than half of the 30 invited to each session showed up.

When the financially unchurched do come, however, the education often takes. Tony Young, 29, a staffer at construction outfit Berry Cos., had put away hardly anything before he attended a session. The newly married Young became a believer and promptly allocated 4% of his paycheck to a 401(k). *Randi Feigenbaum*

IPO TURKEY WATCH

LIFE IS LIKE A LOUSY BOX OF CHOCOLATES

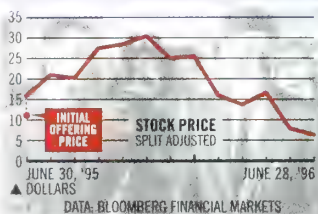
IN *FORREST GUMP*, TOM Hanks's slow-witted hero appears with John F. Kennedy and other long-dead figures, courtesy of Discreet Logic's computerized imaging systems. But Discreet's magic hasn't helped its stock.

Since the Montreal company went public in June, 1995, it fell to 6%—38% off its opening

price and 80% off its high, split-adjusted. The biggest decline came a month ago, when it reported a large (\$15 million) loss and an almost 50% sales drop for its latest quarter.

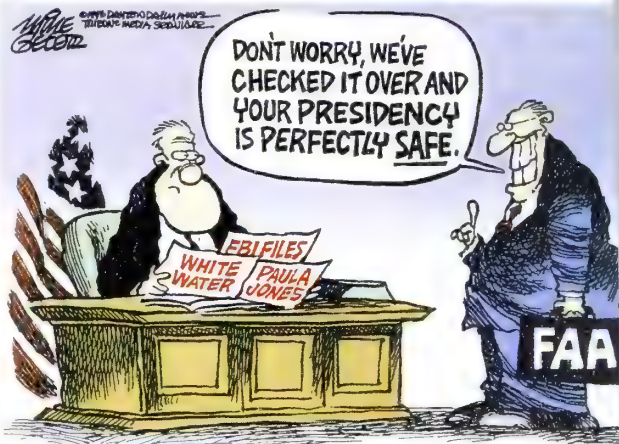
Chief reason: Discreet admits overestimating demand for its main special-effects product, FLAME. And sales of

DISCREET LOGIC PERFORMANCE



DATA: BLOOMBERG FINANCIAL MARKETS

DRAWN & QUARTERED



AFTERLIVES

MR. OUTSIDE IS STILL OUT THERE

IN 1980, JOHN ANDERSON challenged the two-party system as an independent candidate for President. Even though he got only 7% of the vote against Ronald Reagan and Jimmy Carter, Anderson is still pushing for another alternative, though not himself.

Now a constitutional law professor at Nova Southeastern University in Fort Lauderdale, Anderson travels the country giving speeches to church, university, and other groups. He calls for a strong third party to offset too-liberal Democrats and too-conservative Republicans. Voters will hear that a lot from Ross Perot's Reform Party this fall.



ANDERSON
Party po

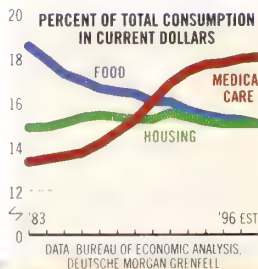
Anderson, 74, is not backing anyone in the 1996 election just yet. He admires former Colorado Governor Richard Lamm, who may run on the Reform ticket if Perot opts out. But Anderson, a former GOP congressman from Illinois, is unhappy that the new party doesn't favor some of his pet issues.

The head of the World Federalist Assn., he wants a powerful international court to resolve disputes leading to wars. And Anderson, also president of the Center for Voting & Democracy advocacy group, urges revamping the electoral system—with fewer U.S. House districts, each electing a batch of members. That would produce more third-party lawmakers, he says. *Randi Feigenbaum*

THE BIG PICTURE

HEALTH-CARE ECONOMY

Time was when Americans paid more for food and shelter than health care. But this decade, because of an aging population and other factors, medical expenses account for the biggest share of each dollar.



DATA: BUREAU OF ECONOMIC ANALYSIS, DEUTSCHE MORGAN GRENELL

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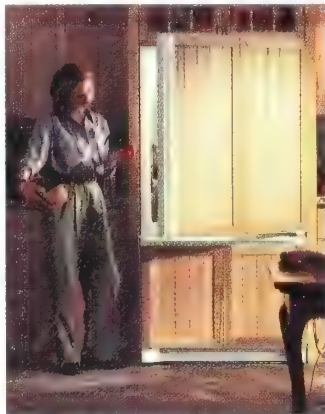
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THE INTERNET: NOTHING TO E-MAIL HOME ABOUT

Your Special Report, "The Information Appliance" (Cover Story, June 24), must have been written by people who've never been on the Internet. Even when you're using a very high-speed personal computer that has the fastest modem available, lots of memory, and a huge hard drive, surfing the Net generally proves to be a frustrating experience.

The bottleneck is not the phone line or the PC. It is the Net itself. The Web is crowded, and there is no control over how many users can access sites or when. Rather than trying to come up with new gizmos, the visionaries ought to be concentrating on getting the Web to work more efficiently.

Rick Cunningham
Chandler, Ariz.

I've been on the threshold of buying a PC any number of times during the past year or so—but I have always said no to myself, mostly because nobody can tell me what it is that I can get off the Web that I can't get out of my daily paper, 40-50 cable channels, the public library, magazines, etc. Until they can, I'll just be a prospect—not a customer.

Richard Trowbridge
Charlotte, N.C.

I read "The Information Appliance" with interest. What you are describing is, in essence, what we in data processing have had for decades: the mainframe (renamed "application server") and terminal (renamed "network computer").

Now, we see the migration back to centralized software servers, on the basis of cost, from the distributed environments so long heralded as the future of information processing. To borrow an adage from the French: "The more things change, the more they stay the same."

Geoffrey K. Wascher
Utica, Mich.

CORRECTIONS & CLARIFICATIONS

In "And the good news is—no comment!" (Up Front, June 24), the name of John Onoda, vice-president for worldwide corporate communications at General Motors Corp., was misspelled.

A NET THAT CAN'T KEEP SECRETS

In "Invoice? What's an invoice?" (Information Processing, June 10), you made only passing reference to the need for adequate data security for the future of electronic commerce. Burdensome federal regulations on data-scrambling technologies—also known as encryption—are threatening the privacy and viability of online communications.

Through unreasonably tight controls on the export of encryption product regulators are preventing the widespread use of adequate encryption. As a result, hackers can easily break into the electronic messages of innocent people.

If financial data, such as credit-card numbers, are not guaranteed adequate security, then the full potential of the Internet and the Global Information Infrastructure may never be realized.

Ed Black
President
Computer & Communication
Industry Assn.
Washington

REMEMBER WHAT THE 'H' STANDS FOR IN HMO

Cheers to Paul Magnusson for his timely, informed suggestions on improving Medicare ("Give Medicare a shot of managed care," Government, June 24). As Magnusson explained, Medicare HMOs can produce dramatic improvements in administrative efficiency. But let us not focus on costs exclusively. It's important to explain that HMOs also offer enormous potential to improve the health of America's seniors.

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Patrick G. Hays
President and CEO
Blue Cross & Blue Shield Assn.
Washington

THE CAVALIER IN JAPAN: TILL A 'CLUNKER'?

Maryann Keller was correct in saying that shipping the Chevrolet Cavalier to Japan was an ill-conceived project from the start ("Is Cavalier Japanese for Edsel?", News: Analysis & Commentary, June 24). A mediocre GM clunker here for some dozen years, the newly dressed model is only a bit improved overall.

Bruce W. Parkinson
San Jose, Calif.

The successful launch of any new product depends on a number of factors, including market conditions. The Cavalier has been on sale for only four months. It is going to take some time to develop public awareness and recognition of this new product. Toyota and GM fully intend to make the Cavalier project a true symbol of successful international corporate cooperation.

Susumu Uchikawa
Board Director
Toyota Motor Corp.
Osaka

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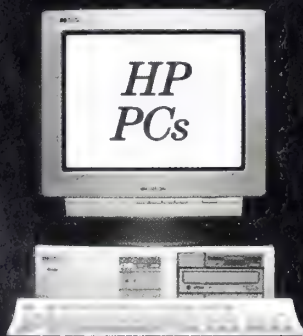
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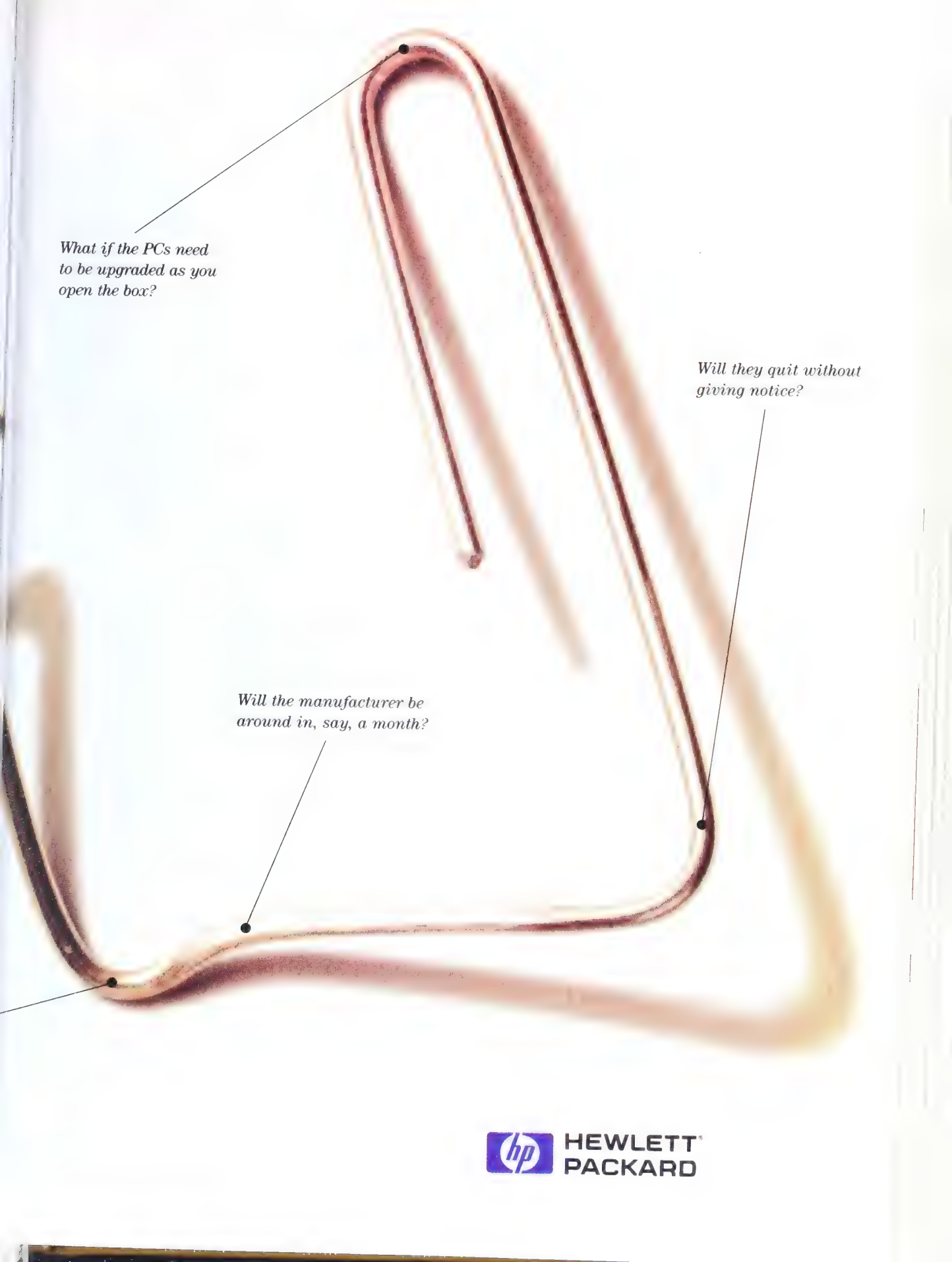
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THE CHOICE

By Bob Woodward
Simon & Schuster • 439pp • \$26

THE BOOK TO READ BEFORE YOU VOTE

Most books about Presidential campaigns are a notebook dump: After election day, exhausted political reporters speed-write coffee-stained notes into a book. The result is usually stale tedium.

Not this one. Instead of waiting until the campaign is old news, *Washington Post* Editor Bob Woodward begins his narrative in late 1994, as a dozen politicians were agonizing about whether to subject themselves and their families to campaign torture. The book concludes on May 15, 1996—174 days before the election—as presumptive GOP nominee Bob Dole quits as Senate Majority Leader to run full-time against President Bill Clinton.

This unusual timing makes the story far more immediate than a campaign rehash. In addition, the book contains headline-generating "revelations," such as Hillary Rodham Clinton's use of spiritual advisers who set up imaginary conversations between the First Lady and Eleanor Roosevelt.

But the most disturbing revelation turns out to be the overwhelming influence that campaign aides wield on policy decisions. Both Clinton and Dole zig and zag on taxes, welfare reform, and balancing the budget. Sometimes, the candidates themselves are confused about who they are. Dole's campaign staff writes major speeches, then demands that the candidate spend hours practicing on a teleprompter. They hope Dole will later automatically read to an audience portions of the speech with which he disagrees. Dole's highly successful May, 1995, attack on Hollywood values had to be practically programmed into a protesting Dole's brain before he would deliver it at a fund-raiser packed with movie and TV moguls.

Clinton is far more eager to reinvent himself. Mindful of the 1994 conservative shift of the electorate, he quietly hires Republican strategist Dick Morris to do

the reprogramming. Morris refers to Clinton's staff as his "jailers," who lock the President into a prison of liberal dogma. Morris, "a shadowy master of circumvention," drafts major speeches, orders up reversals of long-standing foreign and trade policies, and rearranges Clinton's schedule. Puzzled staffers are referred by the President to the newcomer, a mysterious "Charlie" who's there to help organize things.

Woodward catches both the candidates and their staffs while they are under maximum pressure and at their most interesting. Clinton is reeling from the demoralizing 1994 rout of congressional Democrats, who lost the leadership of both Houses after Clinton campaigned heavily for many of the losers. Dole is still bitter about his 1988 primary defeat by George Bush and is worried that time may have passed him by. Avoiding references to his age, 72, is a preoccupation. An aide is instructed that his "number one job in the world is to make sure the guy never falls on ice."

Dole tends to make things worse for himself. He wanders off the message of the day, free-associates during TV interviews, and commits tremendous bloopers—such as telling a Republican audience: "I'm willing to be another Ronald Reagan, if that's what you want." The remark was interpreted as evidence that Dole was insincere. And no wonder. Dole's staff had great difficulty just to get Dole to articulate exactly why he wants to be President.

Since breaking the Watergate story more than two decades ago, Woodward has written a half-dozen other insidey books and has often been criticized for his omniscient style of narrative. The technique, which attributes actual

thoughts to his subjects, is used throughout *The Choice*, which has no footnotes and few hints at sources. I was suspicious of this method until 1994, when I published *The Agenda*, the story of how Clinton formulated an economic policy during his first year in office. One White House aide who had agreed to talk to Woodward for the book confided to me that he and his boss had not planned to reveal much. "But when Woodward came in, it was with a briefcase full of confidential memos we'd written, and any time we said, 'No comment' to a question, he'd pull one of them out and say, 'Didn't you write this?'" I found no one at the White House who disputed the book's details.

Perhaps *The Choice*'s biggest flaw is its reliance on aides to tell so much of the story. Although Dole sat still for 12 hours of interviews, Clinton declined. And while campaign aides might profess loyalty to the boss, most are hired just for the duration, and it is to their

advantage to exaggerate their influence. Morris evidently is Woodward's source for a meeting between Clinton and Morris. Morris recalls Clinton's angry reaction when he tells the President that his aides are leaking news.

Still, Woodward has a fine eye for details and character. For example, Woodward notes that Hillary felt "jerked around by the muddled role of

First Lady, as she swung between New Age feminist and national housewife." Of the incredibly ambitious Senator Phil Gramm (R-Tex.), Woodward writes: "An almost coy smile often rose on one side of his mouth, his head poking out and forward awkwardly like a turtle.... His eyes, deeply set behind his glasses, roamed his surroundings eagerly." No one who knows Gramm could possibly fail to recognize the man immediately. Woodward is also dead-on in his depiction of the chaos, the drama, and the intrigue of an all-out Presidential campaign. It seems an odd way to choose the leader of the free world, but that is the game of American politics.

BY PAUL MAGNUSSON

Magnusson covers economic and social issues from Washington.

THE CHOICE



BOB WOODWARD

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BY STEPHEN H. WILDSTROM

A CHAMELEON OF A LAPTOP

Compaq's Armada can be ultraportable or a brawny multimedia desktop

The big buzz in laptops this summer has been "modular design." In practice, this has meant a laptop that saves space and weight by letting you alter its configuration. You can replace the floppy drive with a CD-ROM drive, for example, or add an extra battery for a long plane flight. But Compaq Computer Corp. is bidding both to redefine the modular concept and to restore its own reputation for innovation. Its new Armada 4100 series can change from ultraportable to multimedia desktop to meet your needs of the moment.

DOUBLE-DUTY BATTERY. The basic Armada is a 5.1-pound ultrathin notebook with a full-size keyboard and an 11.3-in. passive-matrix or brighter 11.8-in. active-matrix display. Its design resembles that of an IBM ThinkPad 560 (BW—June 3). It's a bit thicker and heavier, with a slightly smaller screen—but it's faster than the IBM. Estimated retail prices start at \$2,699 for a passive-matrix, 100-Mhz Pentium unit with 8 megabytes of random-access memory and an 810 MB hard drive. The top-of-the-line 4130T, which I tested, costs \$4,599 with a 133-Mhz Pentium, 16 MB of RAM, and a 1.08-gigabyte hard drive. All models feature 256 kilobytes of "secondary cache," an expensive chunk of superfast RAM often skimped on or eliminated

in laptops such as the ThinkPad 560. Caching is vital to the peak performance of a fast processor, especially in such demanding applications as full-motion video.

This isn't the only area where the Armada outshines the competition. The laptops come with a handle that screws on in seconds and can also be folded under to hold the notebook computer at a comfortable angle for typing. The fat handle weighs nearly a pound because it's actually a second lithium-ion battery. With the handle attached, you can replace the main battery in the laptop with an internal floppy drive. Or you can have both batteries in place and enjoy twice the battery life. Compaq claims 2.5 to 3.3 hours of use for each battery, an estimate that my informal tests suggest is reasonable.

When the battery is doubling as a handle, the Armada 4100 becomes a medium-weight notebook with a lot of battery life but no CD-ROM drive. That's where a mobile CD unit comes in. This \$399, 2.1-lb. device is about the same size as the laptop and a little under an inch thick. It attaches in seconds without tools and provides a quad-speed CD-ROM, bigger speakers, and a bay that can hold a third battery (a \$199 option) or the floppy disk drive. When fully loaded, the Armada 4100 weighs in at a hefty 8.2 lb.—but its weight, thickness, and price are com-

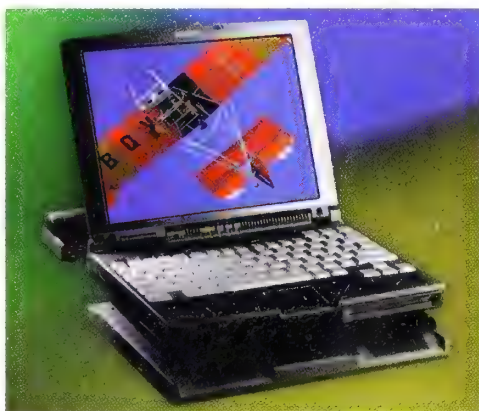
petitive with Toshiba's multimedia Tecra 500CDT.

The Armada isn't out of options yet. This is the sort of laptop that could be your only computer. It's fully equipped, so that you don't need a multimedia docking station. But you can slide the Armada into a "port replicator" that remains permanently connected to a monitor, keyboard, mouse, and other accessories for desktop computers. The replicator comes in two varieties—with Eth-

tested; Compaq promises the problem will be fixed before units reach the market at the end of July.)

If the port replicator is used without the multimedia base and the handle has been removed, a plastic wedge holds the notebook at an angle for greater comfort. The arrangement was easy to connect and use, but it seemed a bit flimsy. Also, the port replicator could be improved by adding a SCSI connector to allow attachment to external

storage devices, such as the increasingly popular Zip and Jaz drive made by Iomega Corp. **QUICK CHANGE.** The protean Armada has one last trick up its sleeve. The built-in mouse substitute is touch-sensitive Alps GlidePad. I find this very handy for word processing and spreadsheet work, but not precise enough for graphic work or for games. I



The Versatile Armada 4100

BASE UNIT

100- to 133-Mhz Pentium; 8- 16-MB RAM; 810-MB-to-1.1-GB hard drive; 5.2 lb., \$2,699-\$4,599

HANDLE/BATTERY

0.9 lb., included in base price

MOBILE CD UNIT

2.1 lb., \$399

THIRD BATTERY

0.8 lb., \$199

PORT REPLICATOR

\$299 with built-in networking, \$189 without

OPTIONAL TRACKBALL

\$49

ernet capability for networking (\$299), and without Ethernet capability (\$189). (Software glitches kept the built-in networking from working on the preproduction unit that I



you need more accuracy, Logitech optical trackball is an option that costs \$49. Interchangeable pointing devices aren't a new idea. But unlike WinBook laptops which require delicate surgery to switch pointers the change on the Compaq takes less than a minute, and the modules seem robust enough that you can change at will without worrying about breaking anything.

Buying a laptop has always meant compromises: features vs. weight vs. battery life vs. cost. Armada's design makes it possible to buy what you need and have what you want when you want it. This summer has produced a bumper crop of innovative laptops, and the

Armada 4100 is the most imaginative departure. It works because Compaq put a lot of thought into making it simple to change configurations on demand. I suspect the design will soon inspire imitators.

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BY ROBERT KUTTNER

WHY A DASH OF INFLATION DOESN'T HURT



TOO RISKY:
A Senate bill
urging "price
stability"
might shore up
your savings.
It might also
swell your
debts and put
millions out
of work

Bob Dole, Senate Majority Leader Trent Lott and 18 other Republican senators are co-sponsors of an eccentric piece of legislation that ought to become an election issue. The bill, whose principal author is Senator Connie Mack (R-Fla.), is titled the Economic Growth & Price Stability Act. It would repeal the 1978 Humphrey-Hawkins Act, which charges the Federal Reserve with maintaining both low inflation and high employment. Instead, Congress would mandate a single goal of monetary policy: "price stability."

This directive would be unprecedented. The Fed's ability to tolerate a bit of inflation to combat recession would be undermined, putting the economy at risk of deflation and depression. The bill reflects several currents of conservative economic thinking. The oldest is Milton Friedman's "natural rate of unemployment." In this view, activist monetary policy cannot change the natural trajectory of the economy. So the Fed should not lean against the economic winds, even during recessions, but rather should target stable growth of the money supply and let business cycles right themselves. Even Alan Greenspan, no liberal, doesn't buy this view. Greenspan's Fed enacted several rate cuts during the last recession.

TRADE-OFF. More recently, theorists have argued that zero inflation is preferable to modest inflation (2% to 3%) on other grounds. Harvard economist Martin Feldstein contends that even slight inflation raises the effective tax rate on capital and thus depresses the incentive to invest. Feldstein's Harvard University colleague, Gregory N. Mankiw, argues that inflation distorts planning for retirement. People's retirement savings will be eroded by inflation, but today's workers don't appreciate the magnitude of that erosion, so they don't save enough. Other economists have long argued that inflation and the fear of inflation distort economic decisions, reduce efficiency, and raise capital costs. Zero inflation would eliminate all these distortions and lead to higher savings, investment, productivity, and growth.

In theory, it's a fine story. However, zero inflation would cause more problems than it would solve. It would worsen the trade-off between inflation and unemployment. According to Brookings Institution economist William T. Dickens, in a recent presentation

to the Jerome Levy Economics Institute, a inflation rate of 3% yields a sustainable unemployment rate of 5.8%, while zero inflation produces a higher jobless rate of 7.5%.

The reason is what economists call nominal wage rigidity. Workers resist cuts in the nominal dollars they are paid, though they do tolerate real wage cuts caused by inflation. Thus, a little inflation allows labor markets to function more flexibly and lets employers take on more workers, who accept small real wage cuts extracted by inflation rather than by the boss. Moreover, according to Brookings' Dickens, countries with low productivity and high unemployment that have sought tight-money cures, such as Canada, have reaped only higher unemployment. Nations such as Germany and Japan, with low but not zero inflation, have been among the best performers.

"DEBT DEFLATION." A moderate amount of inflation, in effect, is a kind of economic lubricant. And contrary to the natural-rate doctrine, there is no evidence that low inflation inexorably mutates into high inflation. Moderate inflation was well-behaved during the 1950s. It rose because of the shocks of the Vietnam War and then OPEC, not because a small amount of inflation fed on itself. Likewise, in the 1990s, low inflation shows no sign of breaking out into high inflation.

If the Fed were required to target absolute price stability, it would be precluded from using monetary policy during economic downturns if the result were even 1% or 2% inflation. The country would be at risk of a "debt deflation," in which debtors find themselves paying off debts in dollars more expensive than the dollars they borrowed. In a general deflation, monetary policy is largely impotent since Treasury securities cannot be issued with negative interest rates. This is the old problem of "pushing on a string."

The sponsors of this bill wrote in a bit of wiggle room. Nowhere do they spell out the meaning of price stability (though the bill implies zero inflation). Rather, the Fed is directed to define price stability and to set a timetable for achieving it. But if the bill means what it says, it is dangerous economic policy. And if it allows the Fed to define price stability as, say, 3% inflation (current policy), the bill is meaningless. Either way, its sponsors are up to mischief.

Robert Kuttner is co-editor of *The American Prospect* and author of *The End of Laissez-Faire*.

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BY MIKE McNAMEE

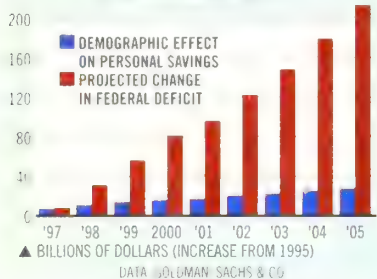
A SISYPHEAN SAVINGS TASK

The rock boomers must roll

Eavesdrop on baby boomers these days, and you'll hear talk of graying hair, bifocals—and mutual funds. Their aging is expected to have an economic bright side: As boomers swell the ranks of the middle aged, they could step up their woefully low savings rate. Indeed, some forecasters predict a demographic bonanza that could boost prices of stocks and other assets to further records.

But those forecasts "run afoul of simple arithmetic," warns economist Ed McKelvey of Goldman, Sachs & Co. The glacial pace of demographic change will

AGING BABY BOOMERS WON'T ADD MUCH TO SAVINGS



make it hard for the personal savings rate to rise from its current 4.5%.

Look at the numbers. Over the next 10 years, the middle aged—those 45 to 64, who tend to save more than other age groups—will grow from 28% of the population to almost 35%. And since they'll be in their peak earning years, boomers' share of national income will rise by 8.1 percentage points—"a seismic upheaval," McKelvey says.

But even with that added income, middle-aged boomers would have to save three times the national average—15% of their income—to raise the overall rate by just one percentage point. In fact, the Labor Dept. reports that 45-to-64-year-olds save about 10%, a tad less than the rate for 35- to 44-year-olds.

The net: At best, demographic changes will add \$27.6 billion to annual personal savings by 2005 (chart). Working against that uncertain progress is another, more likely demographic trend that will bring down savings: rising demand for health care among the aging. Higher spending on Medicare and Med-

icaid is projected to push federal government spending ever higher, raising the deficit from \$164 billion in 1995 to \$376 billion in 2005. For every extra dime the boomers tuck away, Uncle Sam will borrow 76¢. That's hardly the formula for a high-savings economy.

THE PROOF IS IN PERFORMANCE

Affirmative action doesn't hurt

Critics of affirmative action charge that it means companies hire less qualified female and minority workers—and pay a price in poorer performance. New research says they're half-right.

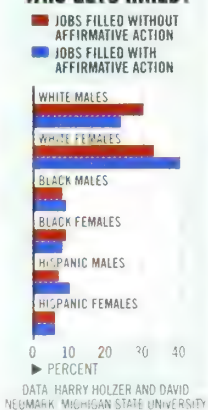
Michigan State University economists Harry Holzer and David Neumark surveyed 800 employers in Atlanta, Boston, Detroit, and Los Angeles between June, 1992, and May, 1994. Each company was asked about its most recent hire. The economists asked about job requirements—especially the education needed—and how well the successful candidate met them.

Some 45% of respondents said affirmative action played a role in their latest hire. And it had a clear effect: White women and black and Hispanic males benefited when affirmative action was used in hiring (chart).

Holzer and Neumark also found that minority workers hired under affirmative action tended to be less well qualified: They had less education than whites hired at similar companies and less than the jobs' stated requirements. Black males hired at affirmative-action companies, for example, had 1.4 years less schooling than white males hired at such companies.

In the workplace, however, the disparities didn't matter much. After some job experience, female and minority workers hired under affirmative action had the same performance ratings as white males. Critics of affirmative action, the economists say, "focus too narrowly on one or two easily observable measures of qualification," and not on "the most important measure—job performance."

AFFIRMATIVE ACTION: WHO GETS HIRED?



WHAT MAKES UNCLE SAM RUN?

New Presidents boost productivity

Efficiency of company workers often rises after a merger or after a new CEO takes charge. The same may be true in the public sector. According to a new study by economist Frank Lichtenberg of Columbia University, government productivity goes up when a new President takes office.

Looking at data from 1967 to 1994, Lichtenberg found that productivity growth was 2.6 times as high in the first year of a Presidency as in its later years. For example, during Reagan's first year in office, executive-branch productivity rose 2.4%, as measured by the Bureau of Labor Statistics. For the remaining seven Reagan years, annual growth was only 0.9%.

One reason for the rise and fall: Executive-branch employment declines by 0.6% during an Administration's first year—but then rises. An inauguration purges the executive branch, notes Lichtenberg, "but as an Administration's tenure increases, fat and inefficiency tend to accumulate."

AS U.S. OVERSEAS DEBT CLIMBS...

...Americans invest more abroad

While U.S. indebtedness to the rest of the world mounts, Americans are investing more overseas—and getting a handsome return on their money. That's the message from Edward E. Yardeni, chief economist at Deutsche Morgan Grenfell/C.J. Lawrence Inc.

Since the Berlin Wall fell in 1989, U.S. investment overseas has soared. Direct investment in companies and facilities abroad hit a record \$96 billion last year, and portfolio investment in foreign stocks and bonds has surged.

Despite the outflow, the U.S. continues to import lots of capital to finance its trade deficits. How? To keep up their exports, many emerging countries have informally pegged their currencies to the dollar, Yardeni says. Defending those exchange rates forces overseas central banks to buy Treasury securities—helping finance both the U.S. budget and trade deficits. So far, the return on Americans' overseas investments is outpacing Treasury rates, Yardeni says—making the swap pay off for the U.S.

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Building for the future...

While on holiday, one family purchased something they couldn't quite manage to bring home... a plot of land for a second home. Word has it that they'll soon be building for their future. "Just something small, enough room for the kids and us... with that glorious scenery outside, who needs a big house?"

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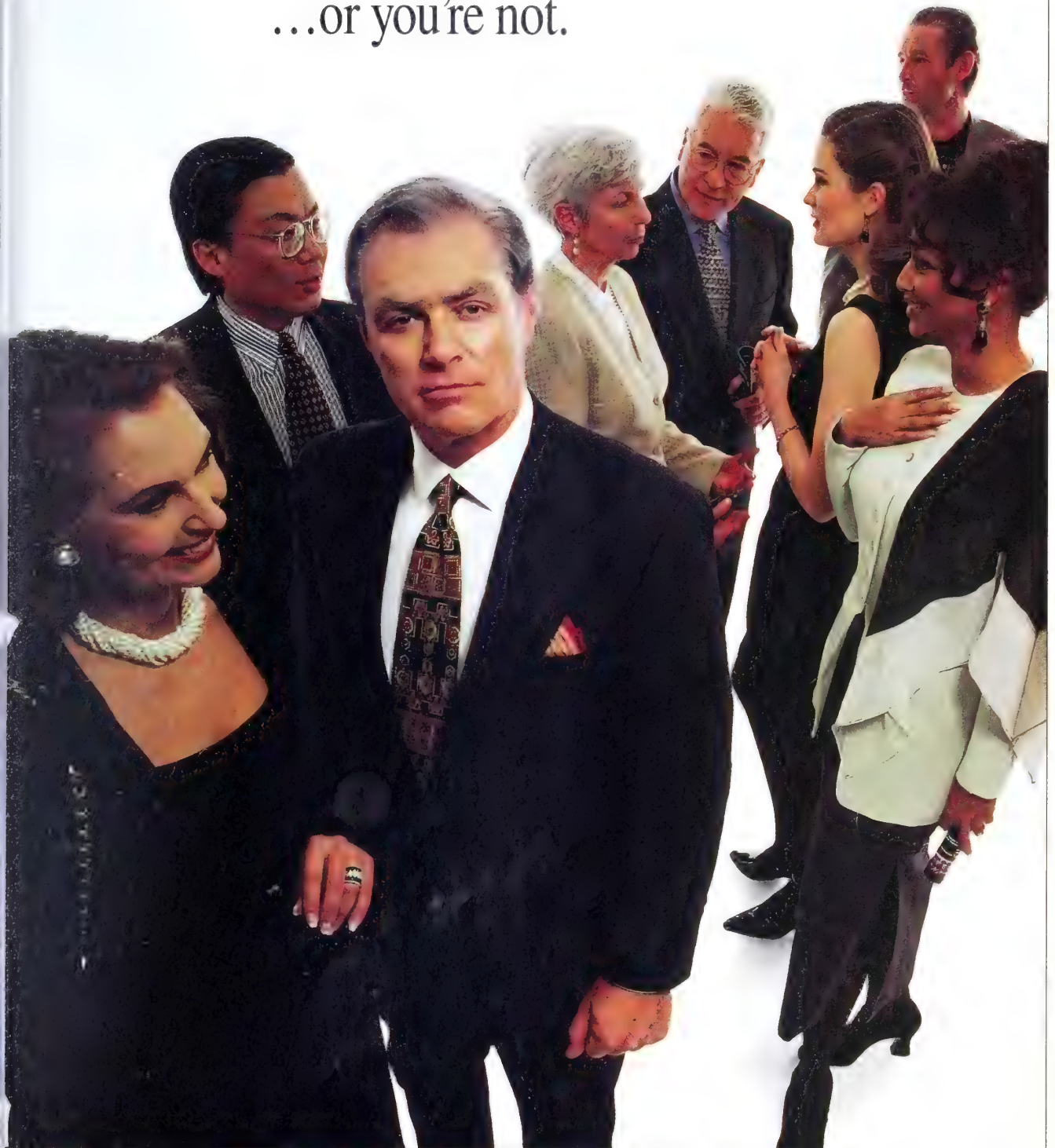




Photo collage print, Atlanta 1996

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JAMES C. COOPER & KATHLEEN MADIGAN

FACTORIES ARE SURGING. WILL INFLATION FOLLOW?

U.S. ECONOMY

Smokestack America is belching fire again. After a strong return in 1994, its best year since the late 1980s, manufacturing struggled last year with stagnant orders and heavy inventories after the Federal Reserve's doubling of short-term interest rates. Output nearly ground to a halt, and factories began laying off workers.

Now, manufacturing's fortunes are changing. After a year of whittling inventories down to size, companies are once again filling order books amid stronger demand, especially by consumers. And the outlook for production gains and new hiring is brightening.

A turnaround at the factory always plays a big role in the outlook because the overall economy is at its healthiest when the industrial sector is on an upswing. The leading indicators are saying as much. The Conference Board's leading index rose 0.3% in May, the fourth increase in a row and the largest four-month rise in more than a decade.

Factory-sector indicators led the May increase.

Manufacturing's new momentum means that some of the economy's second-quarter strength is sure to spill over into the second half. If so, the recent rally in the bond market, which has taken long-term interest rates to below 7% again, may be cut short, as fears of higher inflation take hold. As it stands now, surging May home sales indicate that higher mortgage rates have yet to deter buyers.

AFTER HINTS OF A TURNAROUND

seen in anecdotal reports from industry, including various regional groups of purchasing managers, and a regional survey by the Federal Reserve, clearer evidence of a manufacturing pickup is now surfacing. The National Association of Purchasing Management's index of industrial activity jumped from 49.3 in May to 54.3 in June, the highest level since February, 1995 (chart).

The purchasing managers' index, a composite of several measures of factory activity, strengthened almost across the board. The orders component rose sharply to levels not seen since 1994. Export orders rose, although not as fast as they did in May. Production also picked up, and the employment reading advanced, suggesting that the more than yearlong decline in factory payrolls may be coming to an end.

Another NAPM indicator, known to be one of Fed Chairman Alan Greenspan's pet gauges of future inflation, also rose strongly. The percentage of companies reporting slower delivery times rose for the second month in a row in June. The indicator is a sign of tighter market conditions, which are often a precursor to price hikes and inflation pressures. For now, at least, purchasers report that prices paid to their suppliers actually fell in June.

That could change, of course, if manufacturing's momentum continues to build, and by most evidence it will. Manufacturing appears to be in a classic inventory cycle. After a year in which business inventories outpaced sales, demand is now outstripping stockpiles. So far this year, business inventories have grown at a 2.5% annual rate, down from their 6.3% pace for all of 1995, while business sales are up 4.9%.

Cars and trucks are playing an especially large role in this inventory cycle. After a first-quarter liquidation, carmakers boosted second-quarter output in an effort to rebuild dealers' stocks of vehicles. Amid strong sales in both May and June, Detroit is also lifting its production schedules for the third quarter, which promises to give overall output a boost well into the second half.

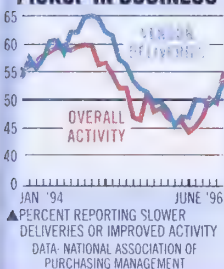
But the inventory swing is not just in autos. The ratio of inventories to sales in manufacturing, wholesaling, and retailing dipped to 1.38 in April, only a shade above the record low of 1.37 plumbed in late 1994. In fact, inventories may be too skimpy in some industries—a sure recipe for increased ordering, output, and employment.

THE REAL SURPRISE

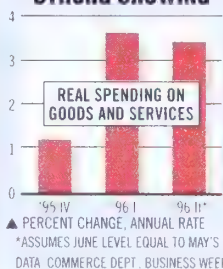
in the manufacturing sector's firmer tone is the unrelenting desire of consumers to keep on spending in the face of higher long-term interest rates, mounting debts, and low savings. Inflation-adjusted consumer spending surged 0.7% in May, mainly on the strength of car sales, which rebounded from an April decline. Overall spending in April was unchanged from March.

The May gain assures another strong quarterly contribution from consumers to economic growth (chart). Even if June spending does not increase, which seems unlikely, second-quarter outlays are on track to match

PURCHASERS SEE A PICKUP IN BUSINESS



CONSUMERS: ANOTHER STRONG SHOWING



Business Outlook

the first quarter's healthy 3.6% growth rate. That's two-thirds of second-quarter real gross domestic product already in the bag.

Consumers were still charging ahead in June as well. Sales of cars and light trucks appear to have been strong, near May's 15.8 million annual rate, which was the strongest of the year.

Consumers' resilience is coming mainly from steady growth in jobs and incomes, and stock market gains have also helped. Although the final installment on President Clinton's tax hike on the wealthy caused real aftertax income to drop 0.8% in April, real income came roaring back in May, rising 1.2%.

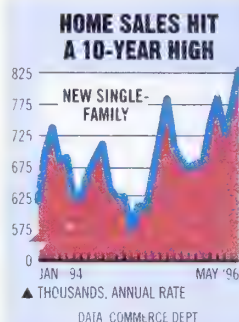
At the current pace of job growth and income gains, consumers can increase their spending at a 2.5%-to-3% pace without drawing down their savings. That's a good thing, since the savings rate was a low 4% in May.

HEALTHY LABOR MARKETS are a big reason why home demand has not yet succumbed to higher mortgage rates. Sales of existing homes rose in May, and purchases of new single-family homes jumped 7.5% in the month to an annual rate of 828,000, the highest sales level in 10 years (chart). Buying was strongest in the Midwest and South. The sales gain cut the supply of unsold homes to a low 5.2 months in May from 5.8 months in April.

Overall construction activity may be reaching plateau, however. But even here, the evidence is mixed and the indicators that are off their recent peaks remain at a high level. For example, although overall construction spending dropped 0.9% in May, it has risen 2% in April, leaving the second-quarter level well above the first three months' mark, so far.

So, too, contracts for new construction fell in May, but remain high. According to F.W. Dodge, a division of The McGraw-Hill Companies, contracts slipped 4% in May, mostly in residential projects. Still, total contracts in the first five months of this year are 6% above the same period in 1995. That means that building activity will slow in the second half of the year, but not collapse.

For now, the data show that factories can count on customers like the construction industry and consumers to keep buying. So the manufacturing resurgence will carry into the second half of the year. The question for Federal Reserve policy as well as market sentiment is whether the busier times on the factory floor will produce price pressures along with the increased output.



CHILE

A POWER SHUFFLE OVER TIGHT MONEY

The sudden resignation of Roberto Zahler, the central bank president, has reignited talk that Chile will ease restrictions on short-term capital inflows. But that move could worsen the inflation outlook.

Zahler's hard line on interest rates conflicted with the government, which was less concerned with fighting inflation than maintaining Chile's roaring growth rate. The index of economic activity—the so-called IMACEC—showed the economy grew by 10.2% in April from a year ago (chart). Chile's real gross domestic product was already up 9% in the year ended in the first quarter. The spurt seems unsustainable, though, given capacity

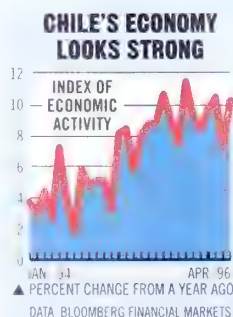
constraints—unemployment was just 6.1% in March—and the central bank's tight monetary policy. Private economists expect real GDP to grow 7.2% for the year, down from 9.6% in 1995.

Trade will slow growth. Exports are flat so far in 1996 and will take a hit from falling copper prices, following the Sumitomo Corp. scandal. Copper accounts for about 40% of Chile's export revenue. Also, imports jumped 22.8% through April. Strong domestic demand means that imports will climb higher. Chile's 1995 trade surplus will slide into deficit this year.

The June 25 announcement that Chile will enter the Mercosur

trade pact, which includes Brazil, Argentina, Paraguay, and Uruguay, on Oct. 1 will help exports begin adding solidly to Chile's growth again. The membership also offers some ammunition against inflation. That's because tariffs on goods from other members—17.4% of Chile's imports—will be cut by 40% and gradually eliminated over the next eight years. Cheaper imports will offset some domestic price increases. The central bank has set an inflation target of 6.5% this year, but in May, inflation was running at 8.6%, up from 8.2% in 1995.

After Zahler's resignation, the central bank said that growth will not prevent inflation from hitting its target. But any easing of capital restrictions now will pump up Chile's financial markets and economy as well as inflation later on.



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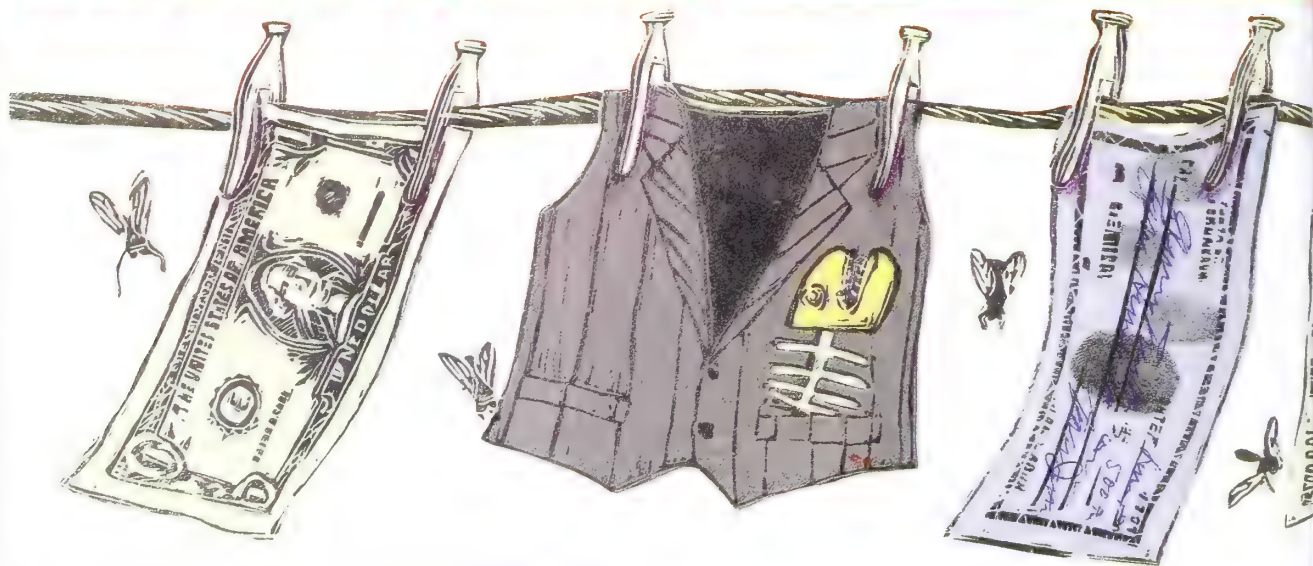
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It's a familiar routine. A scandal erupts at a large corporation. Bowing to public pressure, the board vows to get to the bottom of the mess, hiring a retired government big shot or blue-chip law firm to conduct an "independent" investigation.

Name a major company that's been in trouble recently, and it has probably gone through the drill. On July 1, Bankers Trust Co. released the results of an 18-month investigation into its wayward derivatives group, in which the New York law firm Cadwalader, Wickersham & Taft sharply criticized Bankers for lax internal controls. Mitsubishi Motor Manufacturing of America Ltd. in May asked former Labor Secretary Lynn M. Martin to examine its workplace policies. Her preliminary prescription for combating sexual harassment is due in mid-July. Swedish drug-maker Astra responded to its own sexual harassment scandal two months ago by commissioning a probe by New York law firm Winthrop, Stimson, Putnam & Roberts. On June 26, Astra announced it had fired Chief Executive Lars Bildman and another executive partially as a result of the findings.

A BILLION-DOLLAR INDUSTRY. Not surprisingly, the business of helping companies clean up their acts—a sort of Ethics Inc.—is booming. In June, KPMG Peat Marwick hired Winthrop M. Swenson, a former deputy general counsel at the U.S. Sentencing Commission, to join its new ethics consulting business. Arthur Andersen & Co. started a similar unit last October, choosing author and ex-Harvard University business school professor Barbara Ley Toffler to head its ethics unit. Competitors range from management consultants to law firms and private eye outfits to non-

SCANDALS

ETHICS FOR HIRE

Laundering images of soiled companies

profits such as the Center for Business Ethics in Waltham, Mass. "When you add it all together, you've probably got a billion-dollar industry," says Carole Basri, a Deloitte & Touche ethics consultant.

One reason: Ethics overhauls can be hugely expensive. Orange & Rockland Utilities in Pearl River, N.Y., found that out. In 1993, after running afoul of regulators for widespread financial improprieties, the small utility hired Price Waterhouse and the New Jersey law firm Stier, Anderson & Malone to do an independent investigation. A team of nearly 50 produced a 1,200-page report at a cost of some \$7 million. Consultants charged more than \$200,000 to

design an internal watchdog program. They recommended opening a two-person ethics office at a cost of \$175,000 annually. But Orange & Rockland President Larry S. Brodsky says the investment has paid off: "There's no question that we have regained the confidence of the regulators."

The drill that ethics mavens put companies through varies little. First, the investigation. Then a new corporate code of ethics is generally drafted. Ethics training is beefed up, and a toll-free whistle-blower hot line installed. Then ethics officers are frequently brought aboard to manage the training program and investigate whistle-blower com-

HOW TO CONDUCT AN ETHICS OVERHAUL

Here's the step-by-step approach the pros usually advise

STEP ONE Hire an "independent" investigator to issue a report on the misconduct. Credible former government officials are preferred.

STEP TWO Write a new ethics policy. Deliver document to all company employees with memo from CEO instructing not to ignore it.



ning into big business

complaints. That's the template followed by disgraced companies since the defense-industry billing scandals of the 1980s, and there are signs that some recent victims of notoriety are following suit. Martin says she plans to advise Mitsubishi to increase anti-sexual harassment training, install a monitoring system to track complaints, and hire consultants to review the new programs. Astra has declared it has "zero tolerance" for sexual harassment, slated training for September, and plans to put on an 800 number for ethics complaints.

But does the typical paint-by-numbers corporate ethical overhaul really wipe out malfeasance? Critics contend

that many companies are simply looking for window dressing. "They'll have a code of ethics, but there's no effort by senior management to assure middle management that they really mean it," says Swenson of KPMG Peat Marwick. "They'll do enough training to say that they do training, but they won't really analyze their training techniques to see if they are reaching people. They'll have a hot line, but there's no effort to assure people that there won't be retaliation."

A major problem is that many companies install off-the-shelf ethics programs modeled on federal law, rather than one designed to fix specific problems. In 1991, the U.S. Sentencing

Commission defined seven elements of "an effective [corporate] program to prevent and detect violations of law." The idea was to ensure that companies with strong compliance programs are not unduly fined because of a lone wrongdoer. But companies now often use the law as a rigid map to design their ethics programs. "The federal sentencing guidelines have taken on a life of their own," worries Arthur Andersen's Toffler.

BUYING TIME. Another frequent source of shortcomings in a probe is the "independent" investigator. Some companies have less than honorable motives in mounting an outside investigation, notes Gerald C. Meyers, former CEO of American Motors Corp. First, the probe instantly produces good publicity. It also buys time with regulators, whose chronic understaffing often makes them willing to consider cutting back their own probe if the company's looks reasonably thorough. And doing even a cursory investigation on its own helps the company's legal position. The reason: An outside attorney's findings are generally privileged. Consequently, a company can get a grip on how badly employees behaved and begin assembling its defenses with little risk of disclosure.

But independent investigators have a built-in conflict of interest because they are paid by the company they are supposed to be scrutinizing. And as suppliers of lucrative services to Corporate America, the law and accounting firms that usually run the probes are well aware a reward may be in store if they put the best face on the bad news. "All the biases are to come back with something the company wants to hear," says Meyers. Stanford University Law School professor Ronald J. Gilson contends the

THREE Expand training. Hire consultants, schedule regular sessions on topics such as sexual harassment, bribery, etc.

STEP FOUR Install a whistle-blowers' hotline. Publicize the phone number to employers and establish and detail fully a systematic complaint procedure.

STEP FIVE Hire a full-time ethics officer. It's this person's job to investigate whistle-blower complaints, supervise training programs, and update the ethics policy.

success of an independent probe "all depends on the board."

If the board isn't vigilant, conflicts-of-interest can be glaring: In 1994, a federal court disregarded an ostensibly independent investigation launched by the board of Southern Co., an Atlanta utility holding company, because a law firm that had once represented accused company officers participated in the probe.

COMPUTERS

DIGITAL'S PC PRATFALL

A bungled effort to grow ends in a big charge and layoffs

No. 5 in '95. That was the market-share goal that Enrico Pesatori set for Digital Equipment Corp. when it entered the PC business on his watch in 1993. Pesatori, vice-president and general manager of DEC's computer systems division, had a personal goal, as well: He wanted the top job at Digital.

So much for those plans. Digital badly missed the mark on PCs, racking up an estimated \$200 million loss for the division in the fiscal year ended June 30. Now, Pesatori is out. On July 1, CEO Robert B. Palmer issued a terse statement announcing that DEC's No. 2 executive had resigned.

Bad news for Pesatori. But for Digital, the worst was yet to come. On July 2, Palmer said Digital would cut 7,000 jobs during the next year and take a restructuring charge of \$475 million for the June 30 quarter, putting the full-year profits under pressure. The company's stock declined 12% on the news, to 40%. Coming less than two years into a fragile turnaround for DEC, the drastic moves raise questions about Palmer's long-term strategy and Digital's staying power. "At some point, they are going to end up being forever a niche player," says Lynn Berg, an analyst with Gartner Group Inc.

PRICE WARS. Success in PCs had been an integral part of Palmer's plan. His theory: If Digital could successfully adapt to the falling prices and compressed product cycles of the PC industry, it could apply those lessons to its core computer systems business.

The final dilemma: Even a sincere ethics revamp won't necessarily improve a company's behavior. In a 1995 study, the nonprofit Ethics Resource Center in Washington found that employees at companies with "comprehensive ethics programs" know the law better than workers elsewhere and are more likely to report violations. But they also felt just as much pressure to compromise

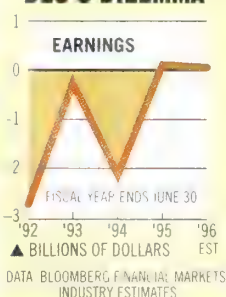
standards in order to meet business objectives and said they witnessed just as much misconduct.

The lesson: Assuring ethical corporate behavior may be a big business. But it's one that has some maturing to do before it proves its full worth.

By Mike France in New York, with Peter Elstrom in Chicago and Mari Maremont in Boston



DEC'S DILEMMA



But under Pesatori's watch, Digital made a series of missteps. Last December, the company poured computers into the distribution channel in anticipation of sales that never developed. Then, with distributors holding 16 weeks of inventory, Digital was forced to take back large numbers of PCs and cut prices on the rest. At the same time, a fierce price war erupted. Digital's PC sales dropped 10% in the quarter that ended in March.

Pesatori, though, refused to alter his strategy of building market share through high-volume shipments, say former Digital PC executives. In a meeting with investors and analysts in March, Pesatori publicly locked horns with Digital Chief Financial Officer Vincent J. Mullarkey over the issue. Mullarkey argued that growth in market share had to come second to profitability.

Pesatori is the third high-ranking Digital executive in the past nine months to leave after profit shortfalls. To some insiders, it's a sign of the drive for accountability that Palmer brought when he became CEO in 1994.

MISSTEPS
With a fragile turnaround less than two years old, drastic moves raise questions about Palmer's long-term strategy

But others contend that Palmer's zero-tolerance policy leads managers to adopt unrealistic targets. "It's a good thing to hold managers accountable," says Berg. "It's another thing not to keep a handle on what's going on in the marketplace."

The PC fiasco raises questions about whether Digital can ever be a major player in PCs. Rival Compaq Computer Corp. has lowered prices by 20% this year, putting smaller players like Digital under enormous strain. "We are a relentless competitor," says Compaq Senior Vice-President Robert W. Stearns. "Only the strong will survive in this business."

Digital's problems aren't all in PCs. Sales of Digital products in Europe, which account for 40% of revenues, are running some \$150 million below expectations. Meanwhile, a strengthening U.S. dollar means currency exchange rates are expected to hurt earnings. What's more, given Digital's anemic 4% revenue growth, some analysts wonder how flagship Alpha systems can be growing at the double-digit rates the company claims. "The company talks about how well it's doing with Alpha," says Merrill Lynch & Co. analyst George D. Ellinger, "yet the numbers don't hold up."

Services, long the company's cash cow, still account for half of Digital's revenues, but profit margins have fallen in the last two years, and analysts say Palmer could sell part of the business. Other units reportedly on the block include Digital's money-losing printer and computer memory divisions.

Palmer told Wall Street that Digital will be back on track in six months. He has taken charge of the computer systems division and plans to run it at least until fall. Says Datapro analyst Peter Lowber: "If they don't do well, Palmer is definitely on the hot seat."

By Paul C. Judge in Boston, with Ira Sager in New York

LOLLAPALOOZA OR HUIZENGA

abbing ADT is a coup—and a boost for his used-car empire

It can't be easy to find a match made in heaven for a company with core businesses in such prosaic areas as waste, burglar alarms, and used cars. But with the \$4.9 billion bid for ADT Inc. on July 1, H. Wayne Huizenga, chairman and CEO of Republic Industries Inc., seems to have found one. The Huizenga team is already gloating. "We've done probably over 10 acquisitions," says even R. Berrard, president and CEO of Republic's AutoNation unit and former head of Block-

buster from No. 7. The goal: take advantage of ADT's strong name in the home security market, which is expanding at 15%-plus annually. With that business booming, Republic can more easily finance its plan to be No. 1 in developing a nationwide chain of used-car megadealerships. Last year, Huizenga founded Fort Lauderdale-based Auto Nation, which in April he sold to Republic for \$250 million. In June, Republic bid \$95 million for CarChoice in Bloomfield Hills, Mich.

ADT may help Huizenga jump-start his used-car op-

hoped the emerging used-car megadealers would never get.

All this put competitors such as CarMax, a unit of Circuit City Superstores Inc., and Driver's Mart Worldwide, a network of big dealers in 31 states, at a disadvantage unless they respond. Predicts Donald L. Keithley, a partner at auto researchers J. D. Power & Associates: "Driver's Mart and CarMax are going to have to start spending serious money to keep up with this."

CAUSE FOR ALARMS? Of course, Huizenga won't be ignoring the opportunities in Republic's other businesses. The deal with ADT will give it a toehold in the retail home security market; ADT has sewn up sales agreements with the Radio Shack unit of Tandy Corp., and a marketing agreement with HFS, the fast-growing franchisor of hotels and real estate brokerages. Republic even sees synergies between the auto and security units, says Berrard: "Think of putting a security system in each car we sell." Huizenga is also building up Republic's

WAYNE'S MULTI-FACETED PLAN

Huizenga's investment group paid over \$100 million for control of Republic in 1995.

Fueled by stock deals, it will near \$2.5 billion in sales in 1996. If the ADT deal goes through, Republic will have several critical strengths:

buster Entertainment corp., "and this is probably the finest fit we've ever done."

It's also Huizenga following his tried-and-true strategy of targeting cash-rich industries ripe for rapid-fire consolidation.

And this time he's got plenty of red-hot Republic stock to fund his acquisition spree. When Huizenga's group paid more than \$100 million for control of Republic in 1995, it was a tiny waste management company. It has since made 18 acquisitions. Now, backed by the reputation Huizenga honed at Blockbuster and waste giant WMX Technologies Inc., its shares trade at an incredible 130 times earnings. The ADT deal catapults Republic to a leadership spot in two of its three core businesses.

In a heartbeat, Republic attains the No. 1 spot in electronic security, with 7 million customers worldwide, up



ELECTRONIC SECURITY

From a tiny base, ADT would make Republic larger than its three biggest rivals combined in the market for home and business security systems. The company would have 1.7 million customers in the U.S., Canada, and Europe.

eration. The company's 29 reconditioning centers save Republic some \$100 million it would have had to spend to turn clunkers into shiny, smooth-running cars. Conveniently, they're located in many of the same sites AutoNation has targeted for

the 80 superstores it intends to open in the next five years. AutoNation will open its first center in Coconut Creek, Fla., in September, although once the CarChoice deal closes, it will have two others in operation.

By acquiring ADT, Republic will gain a direct pipeline to the used and leased cars auto makers sell off by the thousands. That's because ADT is the nation's No. 2 auto auctioneer, behind Manheim Auctions Inc., a unit of Atlanta's Cox Enterprises Inc. "It really gives us a further relationship with suppliers and manufacturers," says Berrard. That's something traditional car dealers had

USED CARS

Since May, Republic has announced stock deals to buy two companies developing superstore chains of used-car dealerships: AutoNation for \$250 million and CarChoice for \$95 million. ADT is the No. 2 auto auctioning outfit in the United States.

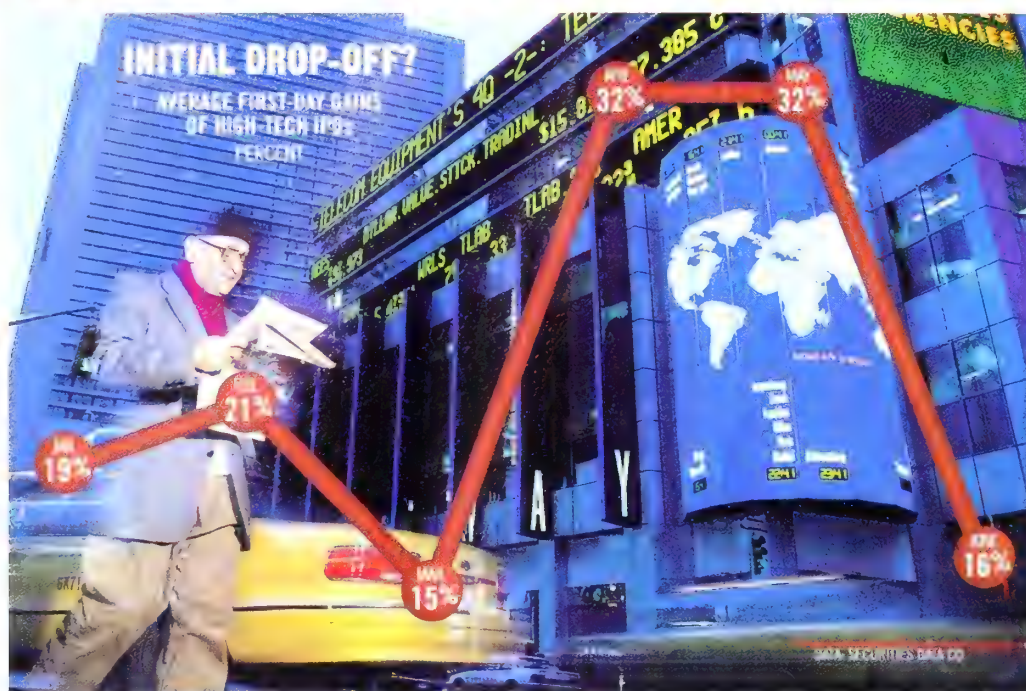
WASTE DISPOSAL

Huizenga wants another shot at his original business (he built up disposal giant WMX Technologies). Republic has paid \$500 million in stock since May for two acquisitions of waste management companies. Disposal revenues should hit \$600 million this year.

waste management business: Just since May, it has paid more than \$500 million to acquire two rivals.

In the meantime, Republic insists the ADT deal will add to rather than dilute earnings this year. Before ADT, Republic's revenues were expected to approach \$1 billion this year. If the deal goes through, investors figure, they'll rise to about \$2.5 billion. But such estimates tend to become outdated quickly in Wayne Huizenga's acquisition-a-minute world. "Most people have been thinking of consolidation as happening at the speed of a baseball game," says Frederick R. Kobrick, a portfolio manager at Boston-based State Street Research, which owns 5 million Republic shares. "But it really happens at the speed of basketball, and these guys play at basketball speed." Now all they need is for ADT to be a slam dunk.

By Jennifer Reingold in New York, with Keith Naughton in Detroit and David Greising in Atlanta



THE MARKETS

THE CYBERSTOCKS THAT FELL TO EARTH

IPO jitters as investors shun companies selling only promise

Peter Norris considers his company lucky. HMT Technology Corp., a Fremont (Calif.) maker of disk-drive parts, had enough cash on hand that on June 18 it could put a planned secondary stock offering on ice. Since investors had pushed its stock down 40%, from 25 to 15, between May 29 when it filed for the offering and June 18, that decision made a lot of sense. "Our fundamentals didn't change," says Norris, HMT's chief financial officer. "But we had to withdraw the offering because of what happened in the market."

HMT is not alone. Ten of 18 technology deals expected during the week of June 24—both initial public offerings and secondary offerings—were either delayed or pulled altogether. Of the 46 IPOs for technology and health-care companies that did hit the market in June, 15 were priced below their expected offering prices. That's compared with just 5 lower-priced deals out of 41 in May, according to an analysis by Robertson, Stephens & Co., a technology investment bank based in San Francisco. Overall, technology and health-care offerings since May 20 have lost 15.5%

of their value since their first day of trading, the firm says.

Suddenly, investors who had hungered for any company with a connection to computers—despite the absence of profits or even actual products—appear to have lost some of their appetite. Amid recent warnings that earnings for established semiconductor companies will be disappointing, they are shunning companies backed by little more than good ideas. "People aren't betting on hope anymore," says Sanford R. Robertson, chairman of Robertson Stephens.

OLD-FASHIONED PROFITS. Hardest-hit have been the flood of Internet-related startups this year. Such stocks are down 24% on average from their opening day of trading, says Securities Data Co. Of six companies offering Internet search tools that have gone public this year, only one, Yahoo! Inc., is trading above its offering price. Broadvision Inc., an Internet software company that went public on June 21, had to reduce its offering price and the number of shares sold. The stock price of VocalTec Ltd., another Internet software company, has fallen from \$19 to \$9 since its February

IPO. "As soon as the speculative froth is off, people start saying I'd rather own Intel than Yahoo!" says Michael Murphy, editor of *California Technology Stock Letter*.

The shifting psychology is apparent in technology-oriented mutual funds. According to AMG Data Services, a firm that tracks mutual-fund investments, technology funds have had net outflows of \$282 million since June 12. Some technology fund managers, once big buyers of new high-tech offerings, are shifting into more tried-and-true investments. Garrett Van Wagoner, head of Van Wagoner Capital Management, with \$1.25 billion in mutual-fund assets, stopped buying tech IPOs two

weeks ago and secondary offerings three weeks ago. "There's way too much supply, and the quality of the IPOs is about as low as you get in a cycle," he says.

Of course, there are plenty of star performers in the technology sector, including Netscape Communications Corp. and Cybercash Inc. And the public is still snapping up the best deals despite the recent downturn. Siebel Systems Inc., a client-server software company that went public on June 28, soared on its first day of trading from \$17 to \$38 per share. But Siebel boasts four straight profitable quarters. "We have old-fashioned things like customers, products, and profits," Chief Executive Thomas M. Siebel says wryly.

Many industry experts are applauding the trend as a way to bring overvalued stock prices back to realistic levels. Yet even with the recent declines, many companies continue to enjoy stock prices that bear no relation to their book values. That is keeping companies such as E*trade Group Inc. and Silicon Gaming Inc. on track to go public this summer. And Wired Ventures Inc., the parent of *Wired* magazine, is planning to sell a minority stake to the public at a price that values the company at \$450 million—yet it has never turned a profit. None of these likely stock issuers seems particularly worried. But, observes Gil Cogan, a venture capitalist: "It's not going to be as much fun as it was." For a while, anyway.

By Linda Himelstein, with Andy Reinhardt and Robert D. Hof, in San Francisco

By Wendy Zellner

DON'T BLOW THIS CHANCE TO OPEN BRITISH SKIES

In any David-and-Goliath battle, it's easy to root for the underdog.

And Richard C. Branson, the scrappy head of Virgin Atlantic Airways Ltd., plays the perfect David. Warning of "monopolistic domination of North Atlantic routes" and higher fares for air travelers, he's pulling out all the stops to kill a proposed alliance between powerhouses American Airlines Inc. and British Airways PLC. In one scathing ad in late June, Branson reminded travelers that American's chairman and chief executive, Robert L. Crandall, once faced antitrust charges after suggesting in a 1982 phone conversation with a competitor that he raise his fares 20% so Crandall could follow suit the next day.

But don't be fooled by Branson's self-serving calls to completely scrap the BA-AA deal. The fact is that it offers the U.S. its best chance in 20 years to pry open the British aviation market, in particular London's coveted Heathrow Airport. That's because British Airways badly wants the proposed partnership to come off and will be prodding British authorities to make it work. That will finally give Britain an incentive to negotiate a more liberal aviation accord with the U.S.

BARGAINING TABLE. As it stands now, only American and United Airlines Inc. can fly to Heathrow under a 1977 treaty. And the British government has the right to review and approve all fare requests. Britain has rejected more fare changes than all other European countries combined, says Patrick V. Murphy, the U.S. Transportation Dept.'s deputy assistant secretary for aviation and international affairs. And the changes Britain nixes often involve rate cuts on flights beyond U.S. gateways. That hardly makes it a consumer's paradise.

The U.S. has moved steadily to bring the British to the bargaining table. By signing "open-skies" accords with 11 other European countries and granting antitrust immuni-

ty to such alliances as Northwest-KLM, United-Lufthansa, and Delta-Swissair-Sabena-Austrian Airlines, U.S. negotiators have been pressuring the British to liberalize their aviation market or watch traffic be drained away from Heathrow by other European hubs.

The hard part now will be hammering out an accord with Britain

American holds 2%. American argues that enough slots can be created for newcomers by better scheduling and runway management. It says that such measures have added more than 70 daily peak-hour slots at the airport since 1992.

SOLUTION. Another solution would be for the British to embrace fully the buying and selling of slots, a practice

common at a few big U.S. airports. If that happened, "the problem would go away in an instant," says Daniel M. Kasper, co-chairman of the transportation industry program at Coopers & Lybrand. "There are a number of Third World carriers at Heathrow who would, with several million dollars in their pockets, gladly change airports" and move to Stansted or Gatwick airports, he says.

Branson has a good point on one issue: antitrust concerns. American and BA together hold 60% of the U.S.-Britain aviation market. To protect consumers on some routes, U.S. regulators will likely have to insist on excep-

tions to the antitrust immunity sought by the two carriers. For instance, the partners would control 100% of nonstop seats between London and Dallas. When the U.S. approved antitrust immunity for Delta Air Lines Inc.'s alliance with Belgium's Sabena World Airlines, Austrian Airlines, and Swissair and United's with Germany's Lufthansa, the Transportation Dept. excluded similar routes, and it should do so again in any American-BA deal.

Done right, an open-skies agreement should mean better service and, at the least, stable fares for consumers. American and BA already acknowledge that the price for their alliance is going to be a U.S. open-skies accord with Britain. The challenge now is how to structure the agreement so consumers—not carping rivals like Branson—get a good deal.

Zellner tracks the airline business from Dallas.



Britain has nixed more fare changes than all other European countries combined

COMPUTERS

UNISYS: NOBODY SAID DIVERSIFYING WAS EASY

Its health-care business is drawing fire in Florida

Like a lot of old-line computer companies, Unisys Corp. is dead set on expanding its position in fast-growing computer-services businesses. In Unisys' case, a major thrust has been into providing computerized health-care services—claims processing and the like—for government employees. Lately, though, that initiative has run into trouble in three states, notably Florida, where authorities have started a criminal investigation of the company.

As recently as January, things looked a lot rosier. Unisys had won a key, \$86 million contract to run Florida's state employee health-insurance business, which took effect on Jan. 1. For Unisys, the contract represented a big opportunity. It has long been in the medical-claims processing business. But in the Florida pact, it was doing more: For the first time, it was responsible for organizing the network of doctors and hospitals and processing claims. Succeeding might help it win other contracts, as states increasingly move to managed care for their employees.

Instead, the Florida contract is in jeopardy. In the first four months of 1996, Unisys was fined \$525,000 for not meeting performance standards, says the Florida Department of Management Services, which says it subtracted the fines from Unisys' average monthly invoice of \$1.1 million. Unisys says it has only been fined a total of \$321,000 for January and February. The big problems: errors and slow response time, the state says. Unisys says it's getting any problems under control.

CRIMINAL PROBE. Now, however, the situation may be taking an even more serious turn. The Florida Law Enforcement Dept. confirms that it is conducting a criminal investigation of Unisys and some employees at the Tallahassee office that handles the contract. "If they've committed anything criminally wrong," says Douglas M. Cook, Director General of the Florida Agency for Health Care Administration, "we would terminate the contract." A spokesman

says Unisys has done its own probe and found "absolutely no wrongdoing."

Part of the state investigation is based on allegations made against Unisys by Scott R. Youngstrand, 30, a onetime claims adjudicator who worked for Unisys for four months. Youngstrand says he was ordered to automatically deny some claims and shift others to electronic mailboxes with different starting dates so Unisys could avoid late fees. When he balked, he says, "I was terminated because I blew the whistle."

Unisys says that Youngstrand was terminated for "poor performance, poor attendance, and inappropriate conduct toward female co-workers"—charges Youngstrand denies. The company says it contacted the state at once upon hearing about the

probe and has supplied records in answer to a subpoena. It also says shifting claims between mailboxes doesn't change the date of the claim.

Other states also are griping about Unisys' handling of traditional claims-processing contracts. Iowa sued Unisys for breach of contract in March, alleging errors in rate-setting. And Kentucky has withheld \$7 million in payments to Unisys because of numerous glitches in the company's handling of a Medicaid claims-processing contract, according to Dee T. Maynard, former executive director of the state's Office of Personnel & Budget. Unisys acknowledges problems in Kentucky but says the Iowa suit has no merit.

"TOTAL CHAOS." In Florida, meanwhile, a state-sponsored review by Coopers & Lybrand, submitted in early May, pinpointed numerous errors and security problems that could lead to breaches of patient confidentiality. State Senator

John Grant has asked the Senate to set up a select committee to look further into the issue. "We're gonna do some extensive investigating," he says.

Another naysayer is Benjamin R. Patterson II, of Patterson & Traynham, attorneys for the American Federation of State, County & Municipal Employees, which plans to sue to rescind the pact. "The folks I've talked to are suggesting total chaos," he says.

The Florida contract may yet work out. Unisys has contracts with other states that are doing just fine. And in cooperation with Florida officials, it has worked out a detailed action plan to remedy remaining problems. One mitigating factor: After Unisys beat out 17-year administrator Blue Cross/Blue Shield of Florida Inc. in July, 1995, Blue Cross appealed and lost. The delay reduced the time Unisys had to get its system up and running.

State officials say they may cancel the contract if things don't improve by late September. "They have made substantial progress," says Cook, "but the jury's still out." If Unisys doesn't fix this contract quickly, it may come away with a badly sullied reputation in health care.

By Jennifer Reingold in New York

Troubling Symptoms

Problems have dogged Unisys since it took over Florida's employee health-insurance business

ERRORS From January through March, a Coopers & Lybrand audit found that Unisys made errors in 8.5% of claims processed, vs. an industry standard of 3.5%. Unisys says its error rate is much lower.

SLOW TURNAROUND In April, only 87% of claims were processed within 30 days, below the 95% required by the contract.

POOR SERVICE Patients say response time is slow and they get conflicting information from Unisys and its subcontractors. Unisys says it's improving communications.

SECURITY PROBLEMS The Coopers audit found significant deficiencies that might allow unauthorized people access to private medical information. Unisys says it is addressing the problem.



PRO AND CON: In a charged climate, mifepristone's maker is saying little

HEALTH CARE

AN INSTANT BUSINESS CALLED THE ABORTION PILL

As the FDA moves toward approval, a startup springs to life

Startups are always fraught with difficulties. But when a company's product is as controversial and revolutionary as the first so-called abortion pill, on track to be approved soon by the Food & Drug Administration, the diversities are far from ordinary.

For Advances in Health Technology, the company awarded the U.S. license to distribute the pill, originally called RU-486, the difficulties "are daunting," says founder Forrest S. Greenslade. Besides scrambling to raise several million in venture capital, company officials have had to contend with fears of violence from abortion foes and with the politics of seeking FDA approval for the drug in an election year. "This company has a lightning rod around it," says Greenslade, who is also the president of IPAS, a group that works to assure safe abortions in developing countries.

Now, despite the hurdles, that work may be paying off. The FDA will hold hearings on the pill, now called mifepristone, on July 19. Capitol Hill insiders predict that if current FDA staffers remain in place after the election, approval could come by yearend.

If successful, mifepristone's path to commercial use could

be a model for other companies seeking to develop new reproductive technologies. Such research has virtually ground to a halt in the U.S. in recent years because of liability concerns and the political controversy created by abortion foes. There are only two major drug companies in the field today, compared with nine in the 1970s.

RU-486 has been a particular target of abortion opponents ever since its approval in France in 1988. Its maker, Roussel Uclaf, at first declined to market it in the U.S. out of fear that abortion foes would boycott other products of its parent, Germany's Hoechst. Finally, in 1993, Roussel bowed to pressure from the Clinton Administration to make RU-486 available in the U.S. and ceded the rights to the nonprofit Population Council, an international re-

productive-health research organization.

Once that deal was completed, RU-486 all but disappeared from the limelight. Then, in late March, the council announced that it had completed clinical trials, submitted an application to the FDA, and licensed mifepristone to one Advances in Health Technology.

TRAINING TEXTS. Amid the political pressure surrounding abortion, the council remains almost obsessively quiet about its work on mifepristone. The group will say only that Washington-based Advances will be involved in providing educational materials and training for clinics and doctors who may prescribe the abortion pill. The president of the company—Dr. Susan S. Allen, a 36-year-old physician who worked previously for the U.S. Agency for International Development in a contraceptive-research program and for Planned Parenthood of the Rocky Mountains—is equally cagey, fearing possible attacks by abortion foes. "I've been in the world of abortion for a while now," she says. "Harassment comes with the territory."

Incorporation papers provide some answers, though, and show that Advances in Health Technology was incorporated on July 12, 1995. Greenslade, who worked at the Population Council until 1991 and helped commercialize the copper-T IUD in 1989, is the incorporating officer. Advances has both nonprofit and for-profit segments. The nonprofit arm will draw up educational materials, and the for-profit part will manufacture and distribute the drug, Greenslade says.

The price has not been announced yet, but industry experts estimate that the treatment will cost about \$50. In all, some 650,000 women annually could use the drug, creating a \$32 million market.

A course of treatment has two stages. First, a woman is given three tablets orally. Two days later, she returns for a dose of another drug, prostaglandin. Some 60% of women expel what Allen calls the "pregnancy tissue" within four hours of taking the prostaglandin. Incomplete expulsions, which occur in 4% or fewer cases, require surgery.

The procedure is unpleasant at best. But for many women, mifepristone may be their best hope for a quiet, safe abortion. If, that is, this startup can successfully bring its first product to market.

*By Naomi Freundlich
in New York*

CLOSE WATCH
The drug's path to market could serve as a model for reproductive-health companies



By Howard Gleckman

A HARD TRUTH ABOUT DEREGULATION

The public outcry following the May 11 crash of ValuJet Flight 592 was both deafening and predictable. First, there was an outpouring of grief for the 110 victims. Then, outrage. The question asked over and over again in recent weeks: How could the Federal Aviation Administration let ValuJet Airlines Inc. fly when the agency knew about safety and maintenance problems at the low-cost carrier?

The answer is simple. The FAA was doing exactly what the public wanted: It gave low-fare, low-cost startups the regulatory flexibility they needed to elbow their way into the market. More than that, the agency's philosophy of cooperating with companies it regulates is what the GOP congressional majority and President Clinton have been demanding of the rest of government. The drumbeat has been relentless: Slash regulation. Curb enforcement. Get the bureaucrats off business' back.

But this new flexibility carries a cost. Nonadversarial government oversight can work fine with companies that have the goodwill, competence, and financial resources to police themselves. It also can pave the way for some to evade the law and put the health, safety, and wallets of the public at risk. Says Massachusetts Institute of Technology Professor and expert on regulation Nicholas A. Ashford: "Accidents are waiting to happen."

COSTLY RULES. Without doubt, deregulation has great advantages. Mindless rules are costly for business and consumers. Regulation restricts competition. Many regs produce little more than paperwork. At the Environmental Protection Agency, for instance, rules often encourage properly filling out forms rather than cutting pollution. "We still need environmental protection," says Terry Davies, director of risk management at Resources for the Future, "but

the system is inefficient, and we spend a lot more than we should."

For a time, the rise of ValuJet was an advertisement for the benefits of deregulation. When regulators let the company farm out maintenance, it could cut costs. That meant cheaper airfares not just at ValuJet but at competitors who slashed ticket prices to stay competitive.



Grief in the Everglades: There's usually a trade-off between economic efficiency and safety

It was just that kind of success that deregulators had in mind as they urged other agencies to adopt similar nonadversarial approaches. The EPA, for instance, slashed enforcement actions by 33% from the third quarter of 1994 to 1995 and has replaced tough crackdowns with "compliance assistance." Echoing the FAA's practice, the environment agency now tries to quietly work out problems with polluters instead of bringing the hammer down on them. In many cases, it works. But it may also increase the odds that some new environmental disaster will explode into the headlines. And then, as happened in 1993 when the parasite *cryptosporidian* contaminated the Milwaukee water supply, killing nearly 100, everyone will ask: How could the government let that happen?

The SEC is another case in point. It

has been struggling to end the widespread practice of Wall Street firms offering brokers free trips and bonuses for hustling in-house mutual funds and other products. Rather than banning the practice with new rules, the SEC is nudging industry to clean up its own act by establishing a model compensation scheme. The result: A half-dozen big firms have ended some

of the most abusive practices. But others have ignored the guidelines. Concedes an SEC official: "The industry as a whole has done too little, too slowly."

SNAKE OIL? This is, of course, nothing new. Congress in 1984 directed the Food & Drug Administration to expand the use of generic knockoffs of brand-name drugs. That brought drug prices down. However, the FDA failed to adequately police the new industry, and some generic makers submitted false data to get their products approved. The scandal sparked a regulatory backlash. Now, the GOP Congress is again pushing the agency toward cooperating with industry. The FDA sometimes approves drugs even though their makers haven't shown that the products actually improve a patient's health. And if Congress further relaxes industry regulations, dangerous products might reach the market.

Demanding 100% risk-protection from regulators, even as we starve their budgets and demoralize their staffs, is insane. The public wants bargain-basement air fares, but no crashes. It demands speedy approval of drugs to care for our children, but is horrified when deaths occur from their effects. Regulators and politicians walk a fine line. And it isn't easy. Perhaps the lesson of ValuJet is this: Neither safety nor economic efficiency comes without a price.

Gleckman follows economic trends from Washington.



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THE OLYMPICS

A NEW OLYMPIC EVENT: GETTING TO WORK

As Atlanta girds for gridlock, companies get creative

On a normal summer day, about 125,000 Atlantans commute downtown in grueling, bumper-to-bumper traffic. Add some 2 million visitors who are expected to descend on Atlanta in mid-July for this summer's Olympic Games, and the picture can be scary. But the longest commute for Douglas G. Thomas, a manager at Atlanta Gas Light Co. will be a 10-minute drive from his home in Suwanee, Ga., to a satellite office. Most days, he'll stay home, communicating with his colleagues via laptop. "I'm looking forward to it. I'll be able to escape from that traffic," he says.

Count Thomas among an estimated 100,000 Atlantans who, during the 17-day Olympic Games, will take part in perhaps the largest-ever mass experiment in telecommuting.

VACATION? Olympic organizers have asked Atlantans to cut local traffic in half during the event, and businesses are scrambling to come up with creative ways to get their employees to work. Rather than cope with that, many employers are simply encouraging workers to work from home, take vacation time, or volunteer at Olympic venues. For instance, about two-thirds of Coca-Cola Co.'s 5,000 or so local employees will be working at the company's Olympic theme park, World of Coca-Cola museum, and pin-trading center, as well as at other Olympic sites.

For those who must get to the office, companies are doing everything

from organizing van pools and hiring private bus companies to running a 6 a.m.-3 p.m. work shift. As Kelly Love, program manager for Commute Connections, a metropolitan-planning outfit, warns: "Coping with the games will be a full-time job for Atlanta businesses."

Executives at Turner Broadcasting Systems Inc. are banking in part on telecommuting to get them through the



STEER CLEAR: For 17 days, the largest-ever experiment in telecommuting

Games. Located at ground zero of the "Olympic Ring," the center of competitive activity, the producer of CNN, Headline News, and the Cartoon Network can't escape the hoopla. To ease the burden, TBS has set up an additional 500 phone lines to allow more than 1,500 employees to work from home. TBS teleworkers can pick up mail and send faxes at a local Mail Boxes Etc. and stay in touch with colleagues through a TBS "intranet"—an electronic bulletin board.

For its 2,000 other employees, TBS has doled out monthly passes for the city's public-transportation system and hired its own shuttle bus.

UPS United Parcel Service Inc. is parking its trucks and asking a small army of brown-uniformed delivery folks to hit the sidewalks. During the games, only 16 drivers will go into the Olympic ring. Instead of driving to their usual 150 different parking locations and 50 dock points, they will each park and unload to 150 UPS "walkers." From there, the walkers will use public transportation to get downtown and will deliver packages on foot. First deliveries will be made at 6 a.m. instead of 10:30 a.m.

Staggered hours alone may not be enough. To avoid traffic jams and street closures, employees at SunTrust Bank

LET THE TRAFFIC JAM BEGIN

How Atlanta companies are dealing with having the Olympics in town

ATLANTA GAS LIGHT Will completely shut down its downtown headquarters. Its nearly 200 employees will work from satellite offices around Atlanta.

BELLSOUTH About 1,000 of its 4,000 employees will telecommute, the rest will commute to downtown, take vacation, or volunteer to work at Olympic venues.

COCA-COLA Will funnel about two-thirds of its 5,000 or so local employees to work at its theme park, Coke museum, and other Olympic sites. The rest will commute to the downtown office.

TURNER BROADCASTING Has hired a private bus company and set up car pools to transport most of its 3,500 employees downtown. The 1,500 employees who plan to telecommute will have access to local mailing and fax points around the city provided by Mail Boxes Etc.

DATA BUSINESS WEEK

Inc., headquartered in downtown Atlanta, plan to work from 6:30 a.m. to 2:30 p.m. Some will have to rise as early as 4 a.m. to get downtown at such an early hour. At the bank's operations center, where checks must be processed as usual, cots are being brought in for employees who can't make it home. For them, as for most native Atlantans, getting through the Games will be a gold-medal feat.

By Nicole Harris, with Kathryn Hayes, in Atlanta

EDITED BY KELLEY HOLLAND

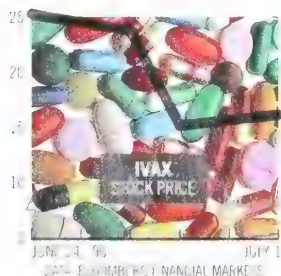
BORLAND'S CHIEF STEPS ASIDE

BORLAND INTERNATIONAL just can't win. The former software highflier has seen revenues diminish every year since 1992 and hasn't turned an annual profit since 1991. On July 2, Borland's president and CEO, Gary Wetsel, abruptly resigned. Wetsel and the company refuse to comment. But UBS Securities analyst Michael Wallace says Borland needs "somebody with a stronger technical background" who can boost corporate sales. Meanwhile, financial woes continue: Also on July 2, Borland warned investors to expect a loss close to \$14 million for the quarter ended June 30. The company expects results to pick up

CLOSING BELL

DRUG OVERDOSE

Forgive Ivax shareholders if they're a bit under the weather. Intense competition in generic drugs, Ivax' main business, prompted the Miami-based company to warn on June 27 that quarterly earnings would come in some 74% under expectations. Ivax stock closed down 8% points that day, at 15%, before recovering to 16% on July 1. CEO Dr. Phillip Frost doesn't have a magic cure. But he sees promise in proprietary products to treat diabetes and bladder disorders that Ivax may soon launch.



when it delivers a new product based on the Internet's Java language. Investors pushed the stock down from 9% to 7% on the news.

LAZARD AUDITIONS MGM SUITORS

IT WILL BE A BUSY JULY 4 holiday for Lazard Frères investment bankers working for Crédit Lyonnais, owner of Hollywood studio MGM. By July 12, Lazard is expected to begin negotiating with a likely buyer. In pole position is PolyGram, a unit of Philips Electronics, with an estimated \$1.3 billion offer. Other bidders include News Corp. and Ace Ventura producer Morgan Creek. MGM is in the midst of a turnaround. But bidders really want its 1,500-film library, including 17 James Bond flicks and classics such as *Some Like It Hot*.

SHAKEUP AT A SWISS BANKING GIANT

HOW TO GET AHEAD IN global banking: build a tightly focused, centrally managed organization. That's why CS Holding, the Zurich-based owner of CS First Boston and Credit Suisse, announced a restructuring on July 2 aimed at consolidating control under Chairman Rainer Gut. The company has been renamed Credit Suisse Group, and deputy Josef Ackermann, who industry sources say moved too slowly with restructuring, is out. Gut has named a new CEO, Lukas Mühlemann, now CEO of insurer Swiss Reinsurance. Gut also is planning cuts in his Swiss retail-banking network.

GOODYEAR DEALERS ARE STOPPED SHORT

GOODYEAR IS NOW OFFICIALLY in the driver's seat in its relations with Goodyear deal-

HEADLINER: STEPHEN TRAFTON

EXPECTING A BIG CHECK FROM UNCLE SAM

On July 1, the Supreme Court handed Stephen Trafton the win of his career. Since taking over as CEO of troubled Glendale Federal Bank in 1992, Trafton poured as much as \$5 million of the S&L's money and untold hours into a high-profile breach-of-contract case against Uncle Sam. Now, the Supreme Court has ruled in his favor.

At issue was the government's decision to rewrite accounting rules for buyouts of troubled thrifts. Trafton argued that the move cost Glendale \$1.5 billion because it forced it to write off \$700 million—from an acquisition

of a failed thrift that the government encouraged—in just six years instead of the 40 the government originally promised.



Cheering from the sidelines are some 120 other S&Ls, some now closed, that have similar suits pending. The government could end up repaying them as much as \$10 billion. The ruling came while Trafton was with his son climbing Colorado's peaks. So he should be in fighting trim for the upcoming damages trial. Says Trafton: "Our ability to be flexible in any settlement is very limited."

By Nanette Byrnes

ers. A federal judge in San Diego ruled for the company on four of five counts on June 28 in a lawsuit brought by dealers who were angry that Goodyear Tire & Rubber was offering name-brand tires to big discounters such as Sears Roebuck and Discount Tire. Still, all is not lost for the dealers. The tiremaker, which has moved to placate dealers with recent marketing steps, wants to put the dispute behind it and is likely to settle the remaining issue.

LUXURY HOTELS IN THE SKY

FORGET UPGRADING TO business class—or even first class. Boeing and General Electric are aiming to offer travelers true luxury with a new version of the Seattle aircraft manufacturer's workhorse 737 model. For a price of \$35 million, Boeing will transform the 120-seat air-

craft into a traveling hotel for CEOs, rock stars, and world leaders. The revamped model could have a lounge area, a private suite, and an office/exercise section, and will carry as many as 60 passengers. Bombardier and Gulfstream Aerospace are already battling in the market for luxury suites in the sky. But with General Electric as a minority partner, Boeing won't be shouldering the risk alone. Look for the new jets by 1998.

ET CETERA...

- General Re, America's largest reinsurer, is buying National Re for \$940 million.
- Lockheed Martin won a \$950 million NASA contract for a reusable rocket.
- Tribune will buy six TV stations from Renaissance Communications for \$1.1 billion.
- A reorganizing Compaq Computer is losing the head of its flagship unit.

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EDITED BY OWEN ULLMANN

REVAMPING THE FDA— WITHOUT THE STRIDENCY

Food & Drug Administration chief David A. Kessler was wary when Representative James C. Greenwood (R-Pa.) called to set up a June meeting. After all, Greenwood was teetering through the House an FDA reform bill that Kessler had testified could put patients and consumers at risk. "You clearly have the votes to ram this through," Kessler pointed out. "Why negotiate with me?"

Greenwood's reply marked a new tack for a Republican party still smarting from the failure of its 1995 revolution. The House had muscled through a staggering number of bills, only to see them gutted or killed in the Senate. Now, the GOP had to prove it could deliver results. "I told Kessler I wanted a bill that he President will sign," Greenwood says. **COMPROMISE.** The upshot: a marathon June 18 session with Kessler that led to several compromises. A revised package due when Congress returns from a holiday recess on July 9 is expected to streamline the FDA's approval of manufacturing processes, give the agency authority to use outside reviewers, and let companies submit summaries of clinical trial data under some circumstances. In addition, it will fix what Greenwood admits were technical errors in the original draft "that could be interpreted as having nefarious results."

There are thorny issues to be resolved. The FDA is balking at the GOP plan to let companies promote unapproved uses for drugs already on the market. And despite a narrowing of differences on drug regulation, the two sides are far apart on medical devices and food. Even so, "there are things that could be worked out so the Republicans could say they have a bill that's passable," concedes a top FDA official.

If the bill becomes law, Greenwood deserves much of the credit. The second-term congressman "is a practical guy, not

an ideologue," explains William W. George, chief executive of Minneapolis medical-device maker Medtronic Inc. "He's the ideal person to work this through the House."

Indeed, Greenwood's approach is a turnaround for the GOP, which made the FDA a favorite whipping boy. House Speaker Newt Gingrich called Kessler a "bully and thug," and other Republicans accused the agency of killing people by being too slow to approve new lifesaving products. When House Commerce Committee Chairman Thomas J. Bliley Jr. (R-Va.) asked Greenwood to head an FDA reform task force in March, the debate was polarized.



GREENWOOD: Pragmatic steps

But the former Bucks County (Pa.) social worker reached out to all sides. "I basically said that to get this done, it has to be bipartisan," he says. Industry execs applauded. "He was really a breath of fresh air," says James S. Benson, senior vice-president of the Health Industry Manufacturers Assn.

CRITICS. That hasn't made Greenwood immune from sniping, however. Democrats say he could have saved time and avoided mistakes by enlisting their help in writing the bill's language. FDA reform advocates fret that he's compromising too much. And industry hands warn that the real power remains with the more conservative Bliley.

Moreover, getting legislation passed this year is uncertain. With only a few legislative days left before the fall election, "our biggest enemy now is the clock," says Greenwood. And when the bill reaches the floor, he may have his hands full fending off amendments to keep the FDA from regulating tobacco or approving abortion drugs.

Still, Greenwood remains optimistic. Even if his efforts fall short this year, he's showing Republicans how they should have gone about their revolution.

By John Carey

CAPITAL WRAPUP

A SICKLY HEALTH BILL

► Senator Edward M. Kennedy (D-Mass.) may kill a health insurance reform bill he has co-sponsored. Reason: his opposition to GOP-backed Medical Savings Accounts. Republican senators offered to limit MSAs to small businesses and the self-employed for a three-year trial. The Joint Committee on Taxation says only 6.1 million of 42 million eligible workers would likely take advantage of the trial. But Kennedy says that's too many. So he's blocking appointment of a conference

panel to iron out differences between House and Senate versions of the reform legislation.

BACK TO BASICS FOR BOB?

► Bob Dole should stop attacking President Clinton's character and stick to pocketbook issues, a new survey suggests. A Harris Poll out July 1 asked 1,008 adults to name the most important issues in voting for President. Only 6% cited character. The top issues: taxes (17%), the economy (14%), health care (12%), the deficit (10%), and abortion (10%).

LORD'S WORK IS DONE

► Assistant Secretary of State Winston Lord, the architect of the Clinton Administration's troubled engagement policy with China, is expected to leave Foggy Bottom early next year. Eager to succeed Lord, Asia policy hands say, is Stanley O. Roth, a former National Security Council deputy for Asia and onetime aide to ex-Representative Stephen J. Solarz (D-N.Y.). Roth currently works at the U.S. Institute of Peace, a Washington foreign policy think tank.

"Sooner or later, something is going to make your hard disk crash."

—FORBES MAGAZINE

COMPUTER APPLICATIONS

EDITED BY DAVID C. CHURBUCK

It could be a power surge, a bad piece of software or your 4-year-old: Sooner or later, something is going to make your hard disk crash. Protect yourself now.

Avoiding disaster

By Steve Kichen

THEORY: A computer's hard disk is utterly reliable. The engineers will tell you that it has a mean time between failures of 300,000 hours. Meaning: If you run your computer for eight hours a day, every day, the disk will crash in the year 2098.

Reality: It could crash next week, wiping out your tax records, your unfinished novel and the software you need to boot up the computer.

Protecting yourself will cost money and take time, but it's a form of insurance well worth having. Some causes of disk failure are easily preventable: a power surge, a brownout or an overheated computer. A basic uninterruptible power supply—which is fine for most home PCs—costs \$100 to \$200 and will run a computer long enough for you to close programs and turn off the system during a power outage. As for overheating, be sure that your computer's ventilation ducts are not blocked; if your computer is crowded with peripheral cards, get a \$20 internal fan card.

Another threat: computer viruses. Commercial viral detection and clean-up software, such as Norton AntiVirus for Windows 95, retails for \$79. In

ing data, the disk could be corrupted. Indeed, there's a chance that you won't be able to start the computer up from that hard disk without correcting the bad data—and of course you can't correct bad data without getting your computer going.

The first thing is to make up a bootable disk—a disk, that is, with enough of the computer's operating system to enable the machine to turn on, get its bearings and listen to further commands. Norton Utilities for Windows 95 (\$130 for the CD-ROM version) includes among its many features a procedure for constructing an emergency boot disk. You

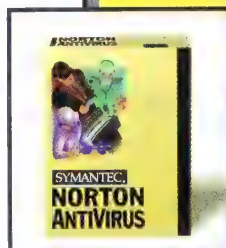
Protection

Disasters happen. In fact, they're more likely than you think. If you access the Internet, or share floppies, you expose your computer to the threat of viruses. If you add new software and files, you could push your computer beyond its limits. Either way, your documents are at risk.

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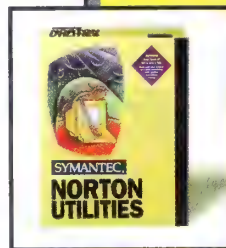
Norton AntiVirus

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MEXICO

CATCHING UP WITH CARLOS SALINAS

The former President talks with BUSINESS WEEK's Geri Smith about his life in exile

No one recognizes the diminutive man as he strolls the historic streets of Dublin, a tweed cap protecting his balding pate. He strides into a hotel bar to greet a visitor, and not one head turns. That's the way Carlos Salinas de Gortari prefers it. For six years, he was one of the most powerful and popular Presidents Mexico ever had. Now, less than two years after leaving office, the 48-year-old Salinas is a pariah in his own land, blamed for everything from its crushing economic crisis to massive corruption scandals. He left Mexico in March, 1995, and has been globe-trotting ever since: six months in New York and Montreal, a few months in Cuba, and now, since spring, a stay in Ireland.

For months, I had been attempting to contact him through his friends and former collaborators. Finally he responded, waking me early one Saturday morning with a phone call to my Mexico City home. We could get together in Ireland to talk, he offered, but he wouldn't say anything that might cause problems for his successor, President Ernesto Zedillo Ponce de León.

I flew to Dublin, and we first met for 2½ hours on the evening of June 25 over Guinness and Heineken at my hotel bar, speaking in Spanish. Coming straight from another appointment, he wore a suit but no tie. A cellular phone attached to his belt rang several times with calls from Irish friends and

a few Mexican acquaintances who still stay in touch. Over drinks that night and dinner the next, Salinas seemed cheerful and upbeat, even though he was aware that recently his image at home had taken another beating. Many Mexicans had watched a CBS *60 Minutes* segment that included a damning summary of the inquiry into the secret Swiss and English bank accounts in which his brother Raúl stashed at least \$110 million.

Raúl has been in jail for 16 months on charges of plotting a political assassination and is now being investigated for alleged "inexplicable enrichment."

He has denied wrongdoing. Prosecutors are looking into whether his Swiss hoard included payoffs from prominent Mexican businessmen who thought they could curry favor or win government contracts by cozying up to the former First Brother. Carlos Salinas is well aware of the damage that the bombshells about Raúl are doing to his once sterling reputation. But when pressed, he declined to



talk on the record about Raúl or what he knew about Raúl's dealings during his six-year presidential term from 1988-1994. Salinas says he is saving his version of events for the Mexican authorities, who apparently have not yet asked him to testify. Although clearly worried about the investigation, he appears confident that his testimony will clear his name.

HARVARD TALK. Salinas also declines to say much about the current economic and political situation in Mexico. He says his silence is his contribution to political stability in Mexico and the imminent economic recovery. In fact, Salinas insisted on limiting his comments to his current activities and refused to be directly quoted even on these.

Still, he seems anxious to dispel any notion that he is skulking around in shadowy exile. He denies he chose Ireland because it has no extradition treaty with Mexico. He says it's because he admires the Irish people, who like Mexicans have suffered under foreign domination or have been forced to emigrate by economic circumstances.

For a former President with no official duties, he seems a fairly busy man. He had just returned from New York, where he attended a meeting of the Dow Jones & Co. board to which he belongs and addressed a select group at the prestigious Council on Foreign Relations. A few weeks earlier, he held a three-day private conference at Harvard University, where he once did graduate work. And two days after our first meeting in Dublin, he was to travel to London on business—although he wouldn't say what for.

The next night, one of Salinas' bodyguards comes by for me and drops me



TRINITY COLLEGE *Salinas enjoys browsing in local bookstores*

ard Rivero, arrives. She is an attractive, articulate 36-year-old economist who met Salinas when she worked for his chief of staff. He recently divorced his first wife and married Gerard. She chats about her studies at Harvard, where last year she earned a master's degree at the John F. Kennedy School of Government, the same place her husband earned a doctorate in 1978.

She is enthusiastically discussing her interest in Cuban history when Salinas comes in. But when she mentions that we had been talking about Cuba, a flash of concern crosses his face. He is apparently worried that she had discussed their recent sojourn there, which he had never publicly confirmed. Salinas seems a bit on edge that night, perhaps con-

he relaxes over dinner, he proudly pulls out photographs of his new daughter, Ana Emilia Margarita, and his three children from his first marriage, who recently visited him in Dublin. Salinas and his new wife seem happy together, occasionally holding hands at the table.

NET SURFER. Salinas fills his days with physical and mental exercise. He enjoys jogging and walking through the streets and browsing through bookshops around Trinity College. He has a few favorite museums, including the Dublin Writers' Museum and the one housing the Book of Kells, a rare 8th century Bible, hand-copied and lavishly decorated by Irish monks. In a land that has produced dozens of important writers, Salinas says he finds ready inspiration for reading, writing, and reflecting. He jots down his thoughts on everything from free-market reforms to social welfare programs, such as the one called Solidarity that he launched while President. He is working on an essay that deals with what he senses is a growing worldwide backlash against economic globalization. But he has not yet decided whether to publish this piece or memoirs of his years in power.

He is in close touch with Mexico, spending several hours a day surfing the Internet, which carries most Mexican newspapers and magazines. Of course, Salinas' life today is far different than what he had expected it would be when he stepped down from power on Dec. 1, 1994. Our last meeting had been in late October of that year, an interview aboard the presidential jet concerning his aspiration to head the new World Trade Organization. Surrounded by aides, a photographer, and even a sound man, Salinas was at the peak of the quasi-imperial

THE NEW DUBLINER Salinas says he chose Ireland because he admires its people and empathizes with its history. He denies he picked it because it has no extradition pact with Mexico

STILL FULL OF IDEAS *Salinas projects the image of a busy man*

at Ernie's Restaurant, an upscale establishment in the tony suburb of Donnybrook. It is nearly empty because everyone is at home watching the England-Germany match of the European soccer championship. But the restaurant has a reservation under the name "Salinas." So I sit down to wait. A few minutes later, his wife, Ana Paula Ger-

cerned about his decision to reveal details of his new life to a journalist. He has reason to be gun-shy. After he had lunch with a prominent Mexican political scientist in Dublin in May, the Mexican press went wild speculating about sinister motives for the meeting.

Salinas appears determined to make the best of his self-imposed exile. Once

power that Mexican Presidents wield. A month and a half later, he completed his six-year term of office with the highest popularity rating ever enjoyed by any Mexican President. Applauded for his efforts to modernize the country's economy and link it to those of the U.S. and Canada in the North American Free Trade Agreement, Salinas was poised to leave office on a high note.

PERFECT SCAPEGOAT. But just three weeks later, the peso collapse tarnished his legacy. Now, Salinas is blamed for everything from too-rapid economic reforms to botched privatizations to possible acts of corruption. Street vendors in Mexico City sell a wide variety of anti-Salinas effigies, ranging from *piñatas* showing him in a tuxedo with pockets stuffed full of money to dolls in prison garb. Mexican newspapers feature insulting cartoons, such as a recent one that shows Salinas, dressed in a leprechaun's costume, sitting on a pot of ill-gotten gold. The exiled President makes a perfect scapegoat.

His close associates believe that once the economy recovers, many Mexicans will realize that many of his reforms, including NAFTA, were worthwhile and ultimately will help the country. But in the meantime, Salinas plans to remain in Ireland. There is much speculation in Mexico that he must move frequently while in exile, hopping from country to country as his visas expire and his welcome wanes. But Salinas says that isn't true. His U.S. visa is good for six months, renewable for an additional six months each time he flies to New York for Dow Jones board meetings. His three-month Irish visa also is renewed automatically, each time he travels elsewhere—something he does often.

As a former President, Salinas is entitled to a pension and lifelong protection by members of the military presidential guard. When he goes out, he is accompanied by one or two discreet plainclothes guards who drive him to appointments in a Rover sedan and a minivan. They travel with him on his overseas jaunts as well.

But the trappings of power seem to end there. Salinas leads a fairly simple life, living with his new family in a rented furnished home in Dublin. When Salinas was President, aides who tried in vain to keep up with his boundless energy called him "Atom Ant." Today, he has slowed down somewhat. But he is still full of energy, ideas, and projects. For now, though, many of them seem overshadowed by the political tempest at home.

By Geri Smith in Dublin

NEW REVELATIONS— AND NEW PRESSURE ON ZEDILLO

While Carlos Salinas de Gortari lives in self-imposed exile in Dublin, new revelations in Mexico threaten to destroy everything he once stood for. Most of these involve his older brother, Raúl, who is charged with masterminding a political murder and inexplicable enrichment. He denies the charges. The huge sums allegedly bestowed on Raúl by Mexico's business Establishment are stoking public anger and cynicism. There is a growing belief that fat cats paid off Raúl to win favors during Carlos Salinas' six-year term. Carlos Salinas has denied knowledge of any such scheme.

The stakes go beyond damage to Carlos Salinas' reputation. These revelations could discredit some of the Salinas administration's most impressive accomplishments, such as the privatization of state companies.

In the latest piece of sensational news, prominent businessman Ricardo Salinas Pliego now acknowledges that he received roughly \$30 million from Raúl. Salinas Pliego got the money at about the time he bought a state-run TV station, Televisión Azteca, from the government for \$628 million. This news has aroused speculation that Raúl is a sleeping partner in Azteca and that other privatization deals were fishy.

"NOT MY PARTNER." Salinas Pliego, who is not related to the Salinas brothers, insists that Raúl gave him the money for investment. He says he bought Mexican stocks for Raúl and then gave him the certificates. He says there was no connection to TV Azteca's privatization. "Raúl Salinas de Gortari is not my partner, he has no shares, nor does he participate... in any company... I hold," said Salinas Pliego in a press release dated June 29.

When news of Raúl's Swiss bank

accounts broke last November, Carlos Salinas issued a statement saying that Raúl should be "firmly punished" if guilty of any wrongdoing. Many Mexicans, though, find it hard to believe that the former President was unaware of Raúl's shenanigans. He certainly was aware that Raúl was engaged in some questionable business practices, a Salinas family source says.

That is why Carlos Salinas pushed Raúl to take a "sabbatical" at the University of California at San

Diego in 1992. But the source denies that Salinas knew about his brother's offshore bank accounts and the hundreds of millions of dollars deposited there. The source suggested that the former President is "very angry" with Raúl for his "excesses."

Carlos Salinas says that he is willing to give testimony to Mexican investigators whenever they wish.

But so far, he has not

been summoned, something that many Mexicans find strange. "It seems obvious to me [that Carlos Salinas should testify] because this is a scandalous situation," says Felipe Calderón Hinojosa, president of the National Action Party, the leading opposition party.

Some observers believe President Ernesto Zedillo Ponce de León is proceeding cautiously for fear of unleashing a witch hunt that could affect influential members of the business community. One of Zedillo's aides counters that Attorney General Antonio Lozano Gracia has been given "free rein" to investigate the Raúl Salinas corruption charges "to their full consequences. He can call anyone he wants to testify, including the former President." As public clamor to get to the bottom of the scandal builds, Carlos Salinas may soon get his chance to explain.

By Geri Smith in Mexico City



SALINAS PLIEGO
A \$30 million puzzle

CHECKING OUT AN OPEL IN WARSAW:
Suddenly, a lot more tires to kick

of the few great growth regions of the world," says David J. Herman, CEO of Adam Opel. "We aim for something more than our fair share."

As foreign auto makers roll in, they're finding customers who are rapidly learning the ins and outs of car buying. After communism collapsed, drivers who once waited years for a junky, state-made Trabant or Skoda were happy to buy any foreign car they could get their hands on. "Nobody knew

which were good and which were bad," recalls Eva, a woman in her 60s, as she browsed in a Daewoo showroom in Budapest. "Now we know what's cheap and reliable."

Price is definitely a major selling point in a market that is only beginning to show signs of affluence. In Poland, the locally made Fiat 126 is a top seller at under \$5,000 and sets the standard by which Poles measure how much a new car should cost. In the Czech Republic, Skoda offers the best price. Thanks to money-saving technology from VW and low Czech wages, Skoda has managed to keep the price of its Felicia as low as \$8,000. While its share is declining, the subcompact still commands 55% of the market, and rivals work hard to compete. "To fight effectively in this country, we must keep our prices in line with Skoda's," says Philippe-Jean Lafond, director of Peugeot's Czech unit.

That even means tailoring new, low-cost models for the region, just as Japanese carmakers have done in Southeast Asia. In Poland, Opel plans to build a stripped-down version of one of its family cars, possibly the Astra, and price it some \$4,000 less than it would cost if made in the West. If the new plant is a success, GM may also choose it to make a new model,



EUROPE

WHAT'S THE TRADE-IN ON A TRABI?

Eastern Europeans are pouring into car showrooms

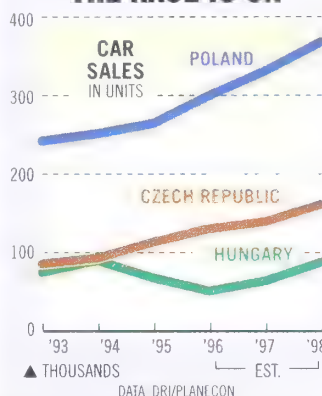
It's Saturday afternoon in Prague, and Jiri Vrba and his wife, Anna, are eyeing a Skoda Felicia in a crowded auto showroom. The \$9,260 subcompact would replace a 20-year-old Skoda they bought secondhand seven years ago that keeps breaking down. From the \$550 a month he takes home as a computer systems analyst and her \$210 as a part-time kindergarten attendant, the couple can just manage a downpayment and five-year financing at 8% interest. Vrba is tempted to stick with a locally made Skoda, now that Volkswagen owns 70% of the company and has introduced better styling and engineering. "It's the best value," he says, loading in his two kids for a test drive. "And no problems about waiting for spare parts."

All across Central Europe, families such as the Vrbas are trading up or buying for the first time. The average age of cars on the road is well over 10 years. But now, robust economies are making people richer, and with inflation and interest rates coming down, borrowing money for big-ticket items is not such a scary prospect. So far this year, new-car sales in Poland and the Czech Republic are up more than 30%

over 1995. Market Researchers at DRI/McGraw-Hill and PlanEcon estimate that regional sales will surge 10% each year through 2000, compared with 2% to 4% in Western Europe. "People would love to replace [their cars] as soon as possible," says Carol Thomas, Eastern Europe auto analyst for DRI.

POLE POSITION. Carmakers from around the globe are rushing to fill the anticipated demand. Poland may be one of the top 10 markets in Europe by the end of the year. That's why Daewoo Corp. pledged \$1.4 billion last year for two plants there and Fiat chose Poland in February for the European production site of the Palio, designed expressly for developing markets. And in late June, General Motors Corp. subsidiary Adam Opel signed off on a plant in Gliwice, in southern Poland, that may build as many as 150,000 cars a year. "It's one

THE RACE IS ON



smaller than Opel's low-end Corsa, that is being considered for developing markets worldwide.

Flexible consumer financing is essential to the growth of this new market. In Poland, for example, banks send agents into the showrooms to process credit applications from prospective buyers. A year after GM started to offer car loans to consumers, a quarter of its Polish transactions are on credit. Vladimir Turek, manager of the largest Skoda showroom in the Czech Republic, offers discounts of up to 15% to those who pay cash. Yet up to two-thirds of his sales are on installment, with many customers dropping by monthly to pay in person. Some Hungarian dealers charge zero interest on the credit line, as long as they receive a hefty down-payment in cash. Budapest Bank, with the help of new owner GE Capital Corp., is making auto financing a top priority.

The dealers are getting help from advertising, but not the kind that features speed and sex. The ads stress safety, reliability, and good value. Those are selling points for motorists who vividly remember driving models down roads strewn with car parts knocked off in minor accidents.

DETROIT EAST? A Skoda ad portrays smiling kids in the back seat, off with the folks to granny's country home—and they get there and back safely on a tank of gas. In a sign of the market's growing importance, foreign auto makers are abandoning their early practice of simply dubbing Western European ads into Polish, Hungarian, or Czech. Daewoo has commissioned a Poland-only campaign from the Lintas ad agency. "With competition heating up, there is a greater need for the right marketing," says Jacek Pilachowski, account executive in Warsaw for Leo Burnett, which created a Polish campaign for Fiat.

For now, it's hard to foresee an end to the region's car boom. That doesn't mean, however, there won't be losers among the auto makers. DRI's Thomas estimates that if car companies build all the factories in the region they have announced, Central and Eastern Europe will end up with annual production capacity of 1.6 million cars by 2000. DRI estimates that's 400,000 more cars than needed for domestic sales or exports to Western Europe. "Someone could get burned," warns Thomas. But not consumers: As price wars heat up, they'll be the winners.

By Karen Lowry Miller in Bonn, with James Drake in Prague, Peggy Simpson in Warsaw, and Rodney Jefferson in Budapest

COMMENTARY

By John Rossant

DON'T LET SAUDI ARABIA BECOME ANOTHER IRAN

As Americans bury the 19 victims of the June 25 explosion in Dhahran, Saudi Arabia, a nightmare is haunting U.S. foreign policy makers. It is Iran. Not in the sense that Tehran may have been involved in the attack, although it is a possibility. Rather, the nightmare is that the House of Saud may be going the way of the Shah of Iran, down and out.

Of course, history never repeats itself in exactly the same way. By the end of his 38-year reign, the Shah had become a desperate and possibly deranged autocrat. The

thousands of ill-educated young Saudis unable to find work in a stagnant economy resent America's close ties to the billionaire Al Saud princes who wield near-total power. Such youths are ripe to become supporters of Islamic clerics pursuing a radical anti-American agenda.

While it is premature to talk about an overthrow, even a crisis in the U.S.-backed House of Saud would make the loss of Iran look like small change. America would be faced with incalculable damage to its global prestige. The demise of Saudi

Arabia's discreet moderation would be bad news for the peace process. Problems in Saudi Arabia, the world's biggest oil exporter, would send shock waves through the global economy.

CORRUPTION. So what can the U.S. do? For one, it can encourage the gradual opening up of the political system.

The lack of a free press and almost any kind of unfettered political debate in Saudi Arabia only contributes to the increasingly religious radicalization of society. The U.S.

should also urge a cleanup of widespread royal-family corruption. Pushing through sorely needed cuts in government spending will be impossible if those at the top are not seen to do their part.

Washington should also insist that the Al Saud resolve the thorny issue of royal succession to avoid potential conflicts among the several hundred princes in line to the throne. Time is getting short, since King Fahd is 75 and in ill health. Crown Prince Abdullah, Fahd's half-brother, is 74.

Saudi Arabia doesn't have to go the way of the Shah's Iran. Given the right mix of prodding and support from the U.S., change can be evolutionary. But as the crescendo of anti-American violence demonstrates, there is no time to lose.

Rome Bureau Manager Rossant covers the Middle East.



MECCA: Will religious fervor threaten stability?

7,000-member House of Saud, by contrast, is anything but a one-man show, and many Al Saud princes still bask in the reflected glory of ancestor Ibn Saud, the charismatic desert warrior who united the Saudi kingdom early in this century. Iran has had a long history of revolutionary agitation and violence, while the only event that brings young Saudis out on the streets these days is a victory by the local football club.

No, Saudi Arabia in 1996 is not Iran in 1976. But the similarities are disturbing enough that Washington should be reformulating its 50-year-old special relationship with the Al Saud. Otherwise, America risks being dragged into a tragic, even bloodier mess. The U.S. Establishment's embrace of the Shah fueled the extreme anti-American policies of Iranian rebels. Today, hundreds of



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TAIWANESE BUSINESS WANTS TO STORM THE MAINLAND

A \$3 billion Formosa Plastics proposal will be a key test case

The chairman of \$10.7 billion Formosa Plastics Corp., Y.C. Wang, has big plans for China. As head of Taiwan's largest private company, he recently asked his government for approval to build a \$3 billion power plant across the Taiwan Strait. That may be just for openers. Speculation is rife that the tough, secretive Wang also aims to build a huge petrochemical complex in China. "The power plant is just a kernel," says one financial analyst in Taipei.

Whatever his grand designs, Wang is stepping up pressure on Taiwan's government to improve ties with China. With both sides cooling their angry rhetoric since March—when Beijing fired missiles near Taiwan and the U.S. Seventh Fleet sailed in—Wang and other Taiwanese executives are pressing Taipei to let them expand economic links with China. "Businesspeople are strongly testing government policy," says David Yu, vice-president of International Investment Trust Co., which runs a Taiwan mutual fund.

President Lee Teng-hui is already showing signs of accommodation. In recent weeks, Taipei has announced a series of measures aimed at improving ties. On July 1, Taipei opened the door to more categories of imports from China via Hong Kong and other channels. The government also eased travel restrictions on Chinese executives. Last month, it gave the O.K. to Taiwanese brokerages to set up research offices in China. And it is going to allow insurance companies to invest there.

OIL ACCORD. Another big step forward was the late June visit of Wang Gui-xiang, chairman of Beijing-based China National Aviation Corp. CNAC last spring gained effective control of Hong Kong Dragon Airlines Ltd., which will start flying to Taiwan next month. Wang, who is also chairman of Air Macau, visited Taipei to complete ticketing agreements with China Airlines Ltd. and Eva Airlines Corp., which will issue tickets to the mainland on Air Macau flights from Taiwan via the Portuguese enclave. That skirts the ban on direct air links. Other

state-sector companies are talking, too: The government-owned oil companies of Taiwan and China recently inked a small but politically significant \$1 million joint venture to explore for offshore oil in the Pearl River basin.

Taiwanese business leaders are hearing reassuring words from their own government. From Lee on down, officials are arguing for reunification in the



NEW LINKS: China's Wang Gui-xiang (right) at a Taipei airline conclave

A WARMING TREND ACROSS THE STRAIT

- Major Taiwanese companies, led by Formosa Plastics, are planning big new investments on the mainland
- Taiwan opens the way for more imports of Chinese products
- Taipei eases travel restrictions on mainland executives
- Airline officials meet to move a step closer to establishment of direct air links

DATA BUSINESS WEEK

long term. Taipei, for example, says it has retreated from its campaign to get into the U.N., a move that would be anathema to Beijing. Instead, many believe the government will focus on attempts to join economic organizations such as the World Bank and the International Monetary Fund.

The Formosa Plastics proposal is a key test of how far Lee's government is willing to go. In 1990, Lee talked Wang out of building a sprawling \$7 billion petrochemical plant in China, persuading the tycoon to build it in Taiwan instead. Today, Taiwanese officials fret that a flood of other corporations would follow Wang to the mainland. "This is [still] negative from a political point of view," says Koong-Lian Kao, vice-chairman of Taiwan's Mainland Affairs Council, a Cabinet-level post. A big outflow of investment could prompt Taiwan "to lose our bargaining power" with China, he adds.

Other companies are pressuring the government as well. Asia Cement Corp., a subsidiary of Far Eastern Group, will apply in July to build a \$240 million ce-

ment factory in China. The company hopes to add a second phase that could cost up to \$200 million. Many companies are be-

coming more open about their investments in China. As of June, 76 companies filed applications to the government disclosing a total of \$1.3 billion indirectly invested in China, up from 41 companies in February. Altogether, the Taiwanese have set up more than 30,000 small and midsize businesses on the mainland.

Opening up big-ticket investments could beef up the island's financial markets. Formosa Plastic's stock has jumped 50% in the past month, buoyed by investors bullish about mainland prospects. Overall, the Taipei stock market is up 40% since February, as optimism increases on cross-strait ties. Investment bankers argue that while Taiwan will experience a short-term outflow of capital by big companies investing in China, international financial institutions will plow money into Taipei stocks perceived as good "China plays," preventing any capital crunch.

For now, at least, Taipei and Beijing have agreed to test the limits of how closely they can knit together their economic interests. There will still be points of friction, to be sure. The two are skirmishing over whether South Africa, the last major country to extend official diplomatic recognition to Taipei, will switch to the mainland. But that is a minor-league spat compared with the threat of war just months ago.

By Joyce Barnathan and Jonathan Moore in Taipei, with Dexter Roberts in Beijing

EDITED BY STANLEY REED

CHINA AND THE U.S. TURN A TEMPEST INTO A TEA PARTY

Acting U.S. Trade Representative Charlene Barshefsky got a special audience after striking an 11th-hour accord on intellectual property rights with officials in Beijing on June 17. She and a few aides were summoned to Zhongnanhai, the official residence of Beijing's party and government leaders.

There, President Jiang Zemin escorted the Clinton negotiator to a quiet room in a traditional Chinese building. Sitting on carved rosewood chairs with pink silk cushions, the two sipped tea and chatted cordially for 40 minutes. To the American delegation, the symbolism was clear. The Chinese were sending a powerful signal that they want to find common ground," suggests a U.S. official.

Indeed, after a gloomy, yearlong string of diplomatic confrontations, both the U.S. and China seem to be rethinking their strategies. Clinton aides have come to see that their China policy was accomplishing little. At the same time, it's clear Beijing's senior leaders realize that without stable ties with the U.S.—China's biggest export market—their economy will be in trouble.

LAGER FOR SUMMITS. Moreover, with Clinton's reelection appearing likely, the Chinese have concluded that a modus vivendi with him is better than four more years of miscues and mistrust. "Both sides have reaffirmed the need for a healthy economic relationship," says Su Ge, a professor of international studies at Beijing's Foreign Affairs College.

Besides patching up differences over intellectual piracy, the two sides also have resolved a dispute over China's sale of nuclear technology to Pakistan. A bid by China's critics on Capitol Hill to yank most-favored-nation trade status for the Middle Kingdom has fizzled. And Beijing is expected to roll out the red carpet for National Security Adviser Anthony

Lake, who arrives on July 6 for wide-ranging talks on security and economic issues. China's Trade Minister, Wu Yi, may be heading to the U.S. in the fall to order jet airliners and other big-ticket items. If the two missions succeed, a new era of cooperation on issues ranging from Taiwan to Korean reunification to arms-trafficking could follow. Marginal improvements in China's human-rights record might even be possible. Both leaders are eager to hold regular summit meetings, perhaps starting next year.

In Washington, Clinton aides say they are quietly shifting from their fuzzy "engagement" approach to *Realpolitik* in China. The Administration says its goal is to work together on common agendas, and that it now intends to deal with China according to "a hard, cold calculus of what our interests are and what their interests are," says a senior U.S. official.

"GRAND BARGAIN." With Lake taking over the lead on China from the State Dept., the Clintonites hope eventually to strike a "grand bargain" with Beijing. The U.S. wants firm commitments from China on such issues as curbing proliferation of nuclear technology and improving human rights. China wants membership in the World Trade Organization and high-profile summits that enhance Beijing's prestige on the world stage.

But improving U.S.-China relations will take time. Renewed tensions over Taiwan or Hong Kong, which returns to Beijing's control on July 1, 1997, are possible. And further showdowns in trade disputes probably are inevitable.

On both sides, though, there seems to be a strong desire not to repeat the past year's confrontations. Barshefsky, Lake & Co. may find themselves sipping more tea in the days ahead.

By Amy Borrus in Washington, with Dexter Roberts in Beijing



CORDIAL: Barshefsky at Jiang's residence

GLOBAL WRAPUP

TURKEY GETS A GOVERNMENT

► An Islamic government is on the verge of taking power in Turkey, a NATO member. But the business community, fed up with months of squabbling, is saying that's better than no government at all. The Istanbul Stock Exchange gained almost 6% in the first three days after the Islamist Refah party formed a coalition with the center-right True Path Party. Should the odd-couple alliance win a July 7 vote of confidence, True Path leaders will control most of the economic ministries.

That, as well as signs that Refah leader Necmettin Erbakan may have moderated his anti-Western economic policies, has calmed investors.

There are signs that foreigners are still bullish on Turkey. Honda Motor announced recently that it will invest \$50 million in a joint venture to manufacture cars.

THAI BANK CLEANUP

► As Prime Minister Banharn Silpa-archa moves to shore up confidence in his handling of the economy, Thailand's central bank governor, Vijit

Supinit, is resigning under pressure. Once regarded as a tough but even-handed watchdog, Vijit presided over a six-month spate of financial scandals. He allegedly accepted shares in a troubled finance company, fired the corruption-fighting head of the Securities & Exchange Commission, and is partly blamed for the failure of Bangkok Bank of Commerce, which collapsed with \$3.1 billion in bad debt. The Prime Minister had already dumped his Finance and Deputy Finance Ministers, who were implicated in some of the same scandals.



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INSIDE MICROSOFT

The untold story of how the Internet forced Bill Gates to reverse course

BY KATHY REBELLO

*Oh, our eyes have seen the glory of the coming of the Net,
We are ramping up our market share, objectives will be met.*

Soon our browser will be everywhere, you ain't seen nothing yet,

We embrace and we extend!

Battle Hymn of the Reorg
Anonymous Microsoft employee
MicroNews, the in-house newsletter

It's nearly 6:30 p.m. on a Friday in mid-May. Microsoft Corp.'s lush campus looks like one of Monet's paintings—a landscape afire with the rich purples and electric pinks of springtime flowers. But no one seems to notice. In the 800-person tools division, where they make products to help developers create software, nearly half the programmers are still hunched over computers, even though for many it's now hour 13 of the workday. Empty cups of espresso and the sleeping bags hooked to the backs of doors speak volumes about the night ahead. And the next night and the next. And probably the next year.

Microsoft, already the ultimate hardcore company, is entering a new dimension. It's called Internet time: a pace so frenetic it's like living dog years—each jammed with the events of

seven normal ones. Microsoft employees are pulling all-

Cover Story

nighters to make up for the precious time the company has lost to Internet go-getters such as Netscape Communications Corp. and Sun Microsystems Inc. "O.K., so we missed the first round of the Internet. Bummer," says Cornelius Willis, Microsoft's product manager for Internet tools. "But we're mobilized now!"

Until six months ago, it looked as if Microsoft might, in fact, be lost in cyberspace. It was so far behind Internet upstarts that industry analysts wondered if the company whose software dominated the PC era might be sidelined in a new age of Internet computing.

It's easy to see how Microsoft might have missed the warning signs. In the early 1990s, while the Net was making its amazing transformation from a nerd's network to a global communications and computing medium, Microsoft was growing explosively, tripling sales, to \$3.8 billion, and boosting its

payroll from 5,600 to 14,400 between 1990 and 1993—all thanks to the success of Windows.

By 1993, techno-hipsters were discovering something called the World Wide Web. It let you display graphics and photos on the Net and most important, let you jump from one Net computer to another by clicking on a highlighted word. At Microsoft headquarters in Redmond, Wash., however, the Net was little more than a curiosity. "I wouldn't say it was clear it was going to explode over the next couple of years," says Chairman William H. Gates III. "If you'd asked me then if most TV ads will have URLs [Web addresses] in them, I would have laughed."

"DRIVING EVERYTHING." Even if Gates and his executives had had an inkling of the Web's trajectory, they had more pressing concerns. Government regulators were in the midst of a huge probe into Microsoft's alleged anticompetitive practices. A hush-hush group was creating a service to rival America Online Inc. Another was building Information Superhighway goodies—video servers for interactive TV, programs for settop boxes, and so on. Most importantly, legions of programmers were jamming to finish what would become Windows 95.

Microsoft's public reaction to the Web remained muted until last fall, when the Web's momentum was too great to ignore—as was the threat to Microsoft. Some 20 million people were surfing the Net without using Microsoft software. Worse, the Web—with a boost from Sun Microsystems' Java programming language—was emerging as a new "platform" to challenge Windows' hegemony on the PC.

Gates had had enough. On Dec. 7, he staged an all-day program for analysts, journalists, and customers to show that Microsoft had every intention of playing—and winning—in the new software game. It would make Web browsers, Web servers, and "Web-ize" existing Microsoft programs. It would even license Sun's Java—whatever it took.

Since then, everybody in Redmond has been on Internet

Until six months ago, Gates & Co. appeared to be lost in cyberspace. But they got religion fast



time. Net projects are under way in every corner of the 35-building campus. The Internet Platform & Tools Div., created in February, has swelled to 2,500 employees—more than Netscape, Yahoo!, and the next five Net upstarts combined. *Slate*, a high-profile Web magazine edited by Michael Kinsley, debuted on June 24. MSNBC, a cable news channel/Web site being produced with NBC Inc., begins on July 15 (page 68). And Microsoft Network will be reborn as a mega-Web site this fall. Says Gates: “The Internet is the most important thing going on for us. It’s driving everything. There is not one product we have where it’s not at the center.”

The impact of those products has yet to be felt, but the speed and intensity of Microsoft’s offensive has already changed

the calculus of competitors and analysts. “People aren’t asking anymore if Microsoft will be killed by the Internet but whether Microsoft will dominate the Internet,” says Scott Winkler, vice-president at market researcher Gartner Group Inc.

Indeed, in just six months, Gates has done what few executives have dared. He has taken a thriving, \$8 billion, 20,000-employee company and done a massive about-face. “I can’t think of one corporation that has had this kind of success and after 20 years, just stopped and decided to reinvent itself from the ground up,” says Jeffrey Katzenberg, a principal of DreamWorks SKG, which has a joint venture with Microsoft. “What they’re doing is decisive, quick, breathtaking.”

Gates, a keen student of business history, has been in-

Cover Story



Our competitors were laughing, said our network was a fake,

Saw the Internet economy as simply theirs to take.

They'll regret the fateful day

The sleeping giant did awake,

We embrace and we extend!

Here, for the first time, is the inside story of Microsoft's dramatic turnabout. It's a tale full of twists, turns, miscues and even a fatefully timed illness. And it's a story of how three young programmers became Net preachers, spreading the gospel and peppering management with E-mail that eventually helped get Gates and his team to act.

LEADING EDGE
Sinofsky, Allard, and Slivka (clockwise from top) peppered management with E-mail about the Net's import

tensely aware of how other market-leading companies—from General Motors Corp. to IBM—have stumbled when their top executives failed to read the signs of fundamental change in their industries. Tackling that problem was a prominent theme in his best-seller, *The Road Ahead*, published last fall. "I don't know of any examples where a leader was totally energized and focused on the new opportunities where they totally missed it," he says.

The Web-izing of Microsoft begins in February, 1994, when Steven Sinofsky, Gates's technical assistant, returned to his alma mater, Cornell University, on a recruiting trip. Snowed in at the Ithaca (N.Y.) airport, he headed back to the Cornell campus. That's when he saw it: students dashing between classes, tapping into terminals, and getting their E-mail and course lists off the Net.

The Internet had spread like wildfire. It was no longer the

Microsoft's Road to the Internet

JANUARY, 1993 Mosaic, the first Web browser, is introduced.

MAY 11, 1993 Bill Gates approves work on Marvel, an online service later called Microsoft Network.

JAN. 25 & FEB. 7, 1994 Two twentysomething Microsoftians, programmer J. Allard and Steven Sinofsky, technical assistant to Gates, send separate memos to manag-

ment warning that Microsoft needs to get jazzed about the Internet.

APR. 4, 1994 Netscape Communications Corp. is founded as Mosaic Communications.

APR. 5, 1994 Microsoft execs hold their first Internet retreat at Shumway Mansion in Kirkland, Wash.

MAY, 1994 Microsoft announces Tiger, a video server for the I-way.

AUG. 15, 1994 Internet evangelist Ben Slivka insists Microsoft develop a browser. The company plans to rush it into Win95.

SEPT. 12, 1994 The first Netscape browser hits the Web.

OCT. 6, 1994 Gates writes a memo called "Sea Change" outlining plans for networked computing.

DEC. 16, 1994 Microsoft licenses Spyglass technology to help it quickly

develop a Web browser.

FEBRUARY, 1995

Paul Maritz writes a memo, "Netscape as New Ware," referring to the Novell software used to run corporate networks. It's intended to show the troops how Netscape will compete with Microsoft.

MAY 23, 1995 Java makes its official debut at the Sun World conference.

MAY 26, 1995 Gates sounds the charge with



work for the technically vy—as it had been seven rs earlier when Sinofsky was dying there—but a tool used students and faculty to communicate with colleagues on ipus and around the world.

dashed off a breathless E-mail message called “Corl is WIRED!” to Gates and his technical staff.

The response from one of Gates’s staff: Someone in working has been “bugging us about this same stuff. ybe you should get together.” The other guy was J. ard. While being recruited in 1991, the cherub-faced grammer had worried whether Microsoft “had a clue out the Internet.” He signed on anyway, figuring he ild help make the company hip to the Net. In 1992, ard was the only Microsoft programmer who had it on business card: Program Manager, Internet Technolo- s. “I was a lonely voice,” he recalls.

ING BUGS. Allard’s job was building TCP/IP, the Net munciations format, into Microsoft LAN Manager and ndows for Workgroups. TCP/IP had long been stand- on the Unix computers made by companies such as n Microsystems. But for Microsoft, says Allard, it s just a “checkbox item”—ordered by Executive Vice- esident Steven A. Ballmer. “I don’t know what it is. I n’t want to know what it is. My customers are scream- g about it. Make the pain go away,” Allard recalls lmer saying.

In an unsanctioned project in early 1993, Allard over- w the development of Microsoft’s first Internet server— computer that could link Microsoft to other Net sites. It is programmed to distribute test copies of the TCP/IP le to customers. Soon, they were posting other bug fixes, and became one of the 10 most-used servers on the Net. Little of this was registering with top management, though. tes, then 37, and his lieutenants had never seen the Net in e way the incoming legions of twentysomethings had. d with so much riding on the Windows rewrite, they had lit- time for new projects.

Allard was increasingly frustrated. The Net was abuzz over

HIGH GEAR Silverberg’s Internet Platform & Tools Div. now has 2,500 workers



Mosaic, a “browser” program created by a precocious computer-science undergraduate at the University of Illinois and posted on the Net for anyone to download. Suddenly, the Web had an easy, point-and-click format—for the masses. On Jan. 25, 1994, he penned a call-to-arms memo titled “Windows: The Next Killer Application for the Internet.”

Allard recommended building a Mosaic-like browser and including TCP/IP in Chicago, the code name for what became



called “The Internet Wave,” which signals changes ahead.

1, 1995 Execs at the Red Lion Inn evue, Wash., for a Internet retreat. the topics: Java.

8, 1995 Net- goes public. Shares rom 28 to 75 before g at 58 the first day.

24, 1995 Win- 5 ships, including re for MSN and the

Internet Explorer browser. **SEPT. 18, 1995**

Netscape introduces Navigator 2.0.

NOV. 6, 1995 Michael Kinsley joins Microsoft to create an online magazine, later called *Slate*.

NOV. 27, 1995 The big browser war begins as Microsoft ships Internet Explorer 2.0.

DEC. 5, 1995 Net- scape’s stock peaks at a stunning 171 (pre-split)

just four months after going public.

DEC. 7-8, 1995 Micro- soft, declaring that “the sleeping giant has awak- ened,” unveils its Net plans—including a plan to use Sun’s Java—at a gather- ing for 300 analysts, cus- tomers, and reporters. In response, Netscape CEO Jim Barksdale jokes: “God is on our side.”

FEB. 12, 1996 Micro- soft ships Internet Infor-

mation Server, a free pro- gram for running Web sites. It will also become part of the Windows NT server software.

FEB. 20, 1996 Inter- net Platform & Tools Div. is created with Brad Sil- verberg in charge.

MAR. 12, 1996 Ameri- ca Online agrees to license Microsoft’s browser. And Microsoft finalizes the Java license deal.

MAR. 25, 1996 Micro-

soft Network hits 1 million customers.

APR. 2, 1996 Micro- soft ships Microsoft Exchange Server, which provides electronic messag- ing, “groupware” functions, and secure Net access.

JUNE 13, 1996 Micro- soft maps out its intranet strategy for major cus- tomers, promising new products including a search engine and a Web- ized version of Office 97.

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INSPIRATION
"The thing that really motivates us is paranoia," says V-P Maritz

Internet. His Apr. 16 memo, "Internet Strategy and Technical Goals," contained the first sign of a growing corporate commitment

"We want to and will invest resources to be a leader in Internet support," wrote Gates.

It was a first step, albeit a measured one. "I don't think he knew how much to bet yet," says Allard. But board member David F. Marquardt did: He recalls that he was "amazed" that Microsoft was putting so little into the Net. "They weren't in Silicon Valley. When you're here, you feel it all around you," says Marquardt, general partner at Technology Venture Investors in Menlo Park, Calif. He broached the subject at the April board meeting that year. Gates's response? "His view was that Internet was free," says Marquardt. "There's no money to be made there. What is that an interesting business?"

To an increasingly important group of competitors, it was clear there was a huge opportunity—and if Microsoft didn't pursue it, they might be able to undo the behemoth's software dominance. Sur-

Slivka proposed that Microsoft give away software on the Na

Win95. This memo also introduced the language that would become Microsoft's battle cry nearly two years later: "Embrace" Internet standards, and "extend" Windows to the Net. Says Allard: "I finally just couldn't take it anymore. I felt the company just didn't get it."

Once Sinofsky weighed in, things started happening. The two began talking, and Sinofsky soon got a Net connection. "I dragged people into my office kicking and screaming," says Sinofsky. "I got people excited about this stuff." Among the infected was Gates. "When Sinofsky started talking about the phenomenon he'd seen at Cornell and [showing] me Gopher and the early Web stuff... it caught my attention," says Gates. "I thought, 'That's a good thing.'"

The boss gave the go-ahead for an executive retreat to discuss the Net. That was a key breakthrough: At Microsoft, such gatherings are convened when Gates feels execs need to focus on a critical issue. On Apr. 5, 1994, two months after Sinofsky's Cornell visit, top brass holed up at the Shumway Mansion in nearby Kirkland, Wash., a 1909 estate used for conferences. Gates and his chiefs pored over a 300-page Internet briefing compiled by Sinofsky. At issue: How important was the Internet? And how much should Microsoft invest in it?

BABY STEPS. In one breakout group, Allard tangled with Russell Siegelman, who was heading Marvel, the code name for what's now the Microsoft Network online service. Allard argued that instead of being proprietary, Marvel should be based on Web standards. Siegelman held his ground—and won. It was a decision that would later cost millions to reverse.

Still, Net progress was made: TCP/IP would be integrated into Win95 and Windows NT, the version of Windows that runs network-server computers. The sales team was told to use the Web to dispense marketing information. The applications group agreed to give Word, the word-processing program, the ability to create Web pages.

Next, Gates jumped deeper into the process by devoting much of his April Think Week—a semiannual retreat—to the

Netscape, Oracle Corp., IBM, and others saw their chance to reset the rules on the Net.

So did the Net startups that were multiplying like cells. Yahoo!, Lycos, InfoSeek, PointCast—dozens were rushing into the vacuum where Microsoft wasn't. The most high-profile of these was headed by James H. Clark, who resigned as chairman of the company he founded, Silicon Graphics Inc., and latched on to the Internet opportunity. He had the goose that laid the golden egg: Marc Andreessen, that 23-year-old University of Illinois programmer. Netscape Communications (originally Mosaic Communications) was founded on Apr. 4, 1994, the eve of the Shumway retreat. By October, it was downloading its Navigator browser across the Internet.

In the spring of 1994, the Net was exploding. Millions of people were logging on. There were some 21,700 commercial Web sites, up from 9,000 in 1991. Even IBM had a home page complete with a greeting from Chairman Louis V. Gerstner Jr. So did General Electric, Tupperware, Volvo, and Hyatt Hotels. Time Warner had Pathfinder, which featured electronic versions of its magazines. Increasingly, the Net, not interactive TV, looked like the route to the Info Highway. Grasping that, Sun Microsystems began adapting a software language for interactive TV into what would become Java.

That April, at the spring Comdex trade show, Sinofsky saw BookLink, a browser owned by CMG Information Services. He showed it to Brad A. Silverberg, then head of Microsoft's Win95 business. Execs began negotiating to license the technology. But as the talks dragged on, AOL swooped in and bought BookLink for \$30 million in November. Says Silverberg: "That woke us up. We had to be a lot more aggressive, a lot more lively. Time was ticking faster in this new world."

During this period, Gates was crafting a strategy for Microsoft in the emerging wired world. But as outlined in his October, 1994, memo, "Sea Change," the approach was to use existing Microsoft products. Other Microsoftians were becoming convinced that the Internet was the way.

One was Benjamin W. Slivka, now 35 and project leader for Internet Explorer, Microsoft's browser. In mid-1994, he and other programmers were looking into what features to put in for the successor to Win95. He got his Internet hookup and soon knew the answer: On Aug. 15, he sent E-mail to his all hand, saying they needed a browser and might even get it ready for Win95. When Netscape's Navigator hit the Net that fall, Slivka checked it out, then grabbed six people and popped out the browser features for Win95.

To get the work done faster, one of his programmers took a sopping trip—to Spyglass Inc. in Naperville, Ill., a Netscape rival. It was an ironic moment for Spyglass CEO Douglas P. Colth. Six months earlier, he had come calling on Microsoft—only to be rebuffed. "Typically, they said, 'We'll build it ourselves,'" says Colbeth. But by late 1994, Netscape was gaining its ascent and Microsoft was eager to deal. It signed Spyglass license on Dec. 16.

WORK NEWS. Still, going into 1995, Microsoft management is focused on Chicago. Originally scheduled for December, 1994, it had been pushed back to mid-1995 and would emerge, finally, as Win95 that August. The company was scrambling to complete Windows NT for the corporate market, too. "Those are the focus," says Gates, "and the Internet was like an underlying rumble."

Gates had also ordered that Microsoft Network should make debut with Chicago. The MSN story is loaded with might-have-beens. In December, 1992, when Siegelman started the planning, the Net was hardly a showstopper. The real star was UUNET, a Windows-based online service that was gaining members

persuaded Tele-Communications Inc. to pony up \$125 million for a 20% stake in MSN. TCI chief John C. Malone had been on the verge of investing that amount in rival AOL. But, says AOL CEO Steven M. Case, "in the final hour, Gates persuaded him—implored him—not to invest in AOL." Three weeks later, Microsoft paid \$16.4 million for 15% of UUNET Technologies Inc., which now carries MSN traffic.

Despite MSN, by May, 1995, Gates was sounding the Internet alarm. He issued "The Internet Tidal Wave," a memo that hit on the themes that had been reverberating throughout Silicon Valley. He declared that the Net was the "most important single development" since the IBM PC. "I have gone through several stages of increasing my views of its importance. Now, I assign the Internet the highest level," he wrote.

On May 27, Slivka issued his own alarm, titled "The Web Is the Next Platform." He warned that the Web had the potential to supersede Windows. Says Slivka: "I don't know if I actually believed that would happen. But I wanted to make a point."

There was a growing sense among Microsoft execs that the Internet opportunity had to be seized—before it slipped to others. On June 1, 40 of them gathered at the Red Lion Inn in Bellevue, Wash., to brainstorm Net strategy. Gates gave a 20-minute talk on the "Internet Tidal Wave." Slivka's scheduled 15-minute talk ended up lasting more than an hour: "I got some people riled up," he says. At one point, Slivka proposed that Microsoft give away some software on the Net, as Netscape was doing. Gates, he recalls, "called me a communist."

Cover Story

a Netscape. Gates, as he recalls, "called me a communist"

a rapid clip. So in May, 1993, Gates approved Siegelman's plan for a rival service that would have a big advantage—the software needed to use it would be included in Win95.

In the fall of 1993, the MSN team ramped up to get done in time to come out with Chicago. But, heeding the Net rumors, Gates agreed to let Rob Glaser, a longtime Microsoft executive who had pioneered the push into multimedia, do an analysis of how the Net affected MSN. His conclusion: Microsoft should "radically change" the strategy and make the online service part of the Net.

Then, fate stepped in. In November, 1993, Siegelman, now 34, suffered a brain hemorrhage. He would recover, but his absence prompted the normally relentless Glaser to ease up. He presented his plan to Siegelman's staff, but with the boss away and the team already stressed out, he didn't push hard. "We just couldn't afford to spend a lot of energy changing our plan," says Jeffrey Lill, a former MSN team member. Adds Glaser: "I felt the stars were not aligning for Microsoft to really understand the Net early."

Besides, MSN was a high-profile project. Gates unveiled the planned service in a keynote speech at Comdex in November, 1994, and within weeks

Executives also went through every Net project that Microsoft had in the works and got their first peek at Java. The reaction? "Like the early reaction to my memo, it was lukewarm," says Allard.

Only after Win95 was shipping in August did Microsoft put full force into the Net. "In the three or four months before,

there were symptoms that this thing was really accelerating," says Gates. "I said, 'O.K., once we get Windows 95 shipped, I'm really going to put a lot of thinking into how this affects our strategy. Can we have a strategy where we bet on the Internet and assume it's really going to drive demand for PCs and software? And how would that reshape our strategy?'"

Gates had no time to lose. On Aug. 8, 1995, Netscape seized the spotlight with a spectacular initial public offering—which soared from 28 to 58 the first day and launched a bull market in Internet stocks. Chairman Clark became a paper billionaire 18 months after launching his company. Gates didn't hit that milestone until Microsoft was 12 years old.

Netscape was gaining more than a following on Wall Street. It had Microsoft-like dominance in the Web-browser business and was signing up blue-chip customers who were

Buying the Parts for a Net Strategy

Microsoft has been buying up promising Web startups to help it move more quickly onto the Net

- JAN. 13, 1995** Takes a stake in UUNET Technologies Inc., an Internet service provider that will provide Internet access for Microsoft Network.
- JAN. 16, 1996** Buys Vermeer Technologies Inc., the Cambridge (Mass.) maker of FrontPage, a tool for creating and managing Web documents.
- MAR. 12, 1996** Acquires Colusa Software Inc., maker of Omnware, which is used to make object-oriented programming that runs on the Internet.
- JUNE 11, 1996** Buys eShop Inc., a leader in Internet commerce software, for under \$50 million. eShop's technology will become a key part of Microsoft's Merchant software for electronic retailing.
- JUNE 17, 1996** Acquires Electric Gravity Inc. Its Internet Gaming Zone, which features multiplayer games such as chess and bridge, will be linked to the Microsoft Network.

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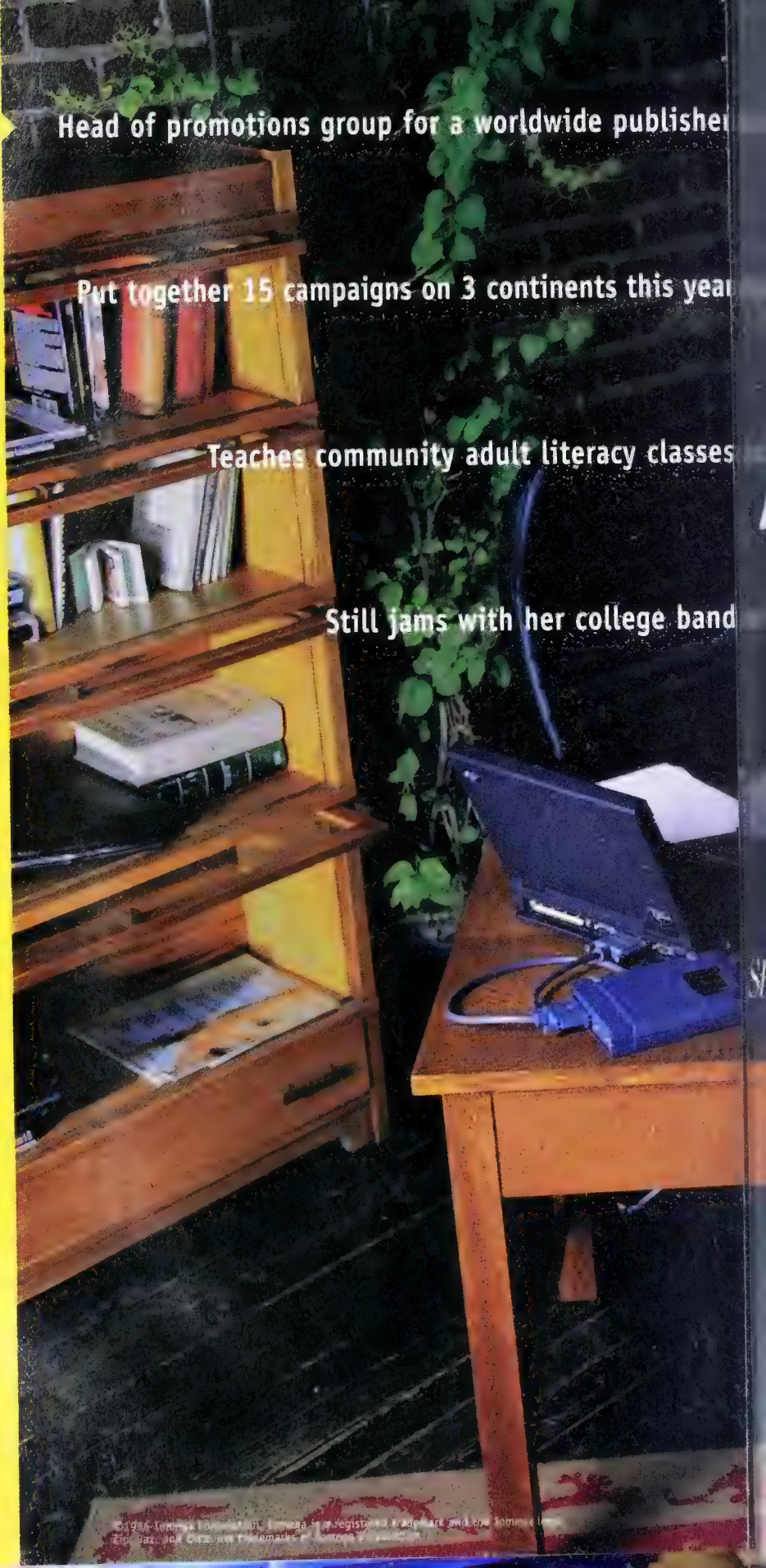
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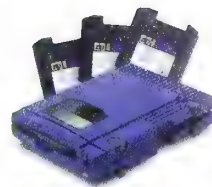
Still jams with her college band





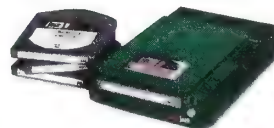
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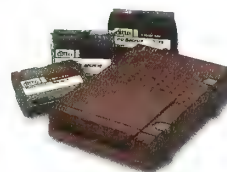
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On the eve of the Net summit, Gates slumped to the floor, exhausted. No one knew if he was furious or just thinking

building Web sites with the Netscape server program. Meanwhile, all of computerdom was getting jazzed about Java, the Sun software that would make it possible to zap programs as well as Web pages over the Net. That scheme threatened to make the Web a place where Windows mattered not at all. On

Nov. 16, Goldman, Sachs & Co. removed Microsoft's stock from its "recommended for

Cover Story

purchase" list because of Internet concerns. The message was clear: If Microsoft didn't want to be eclipsed in the network-computing era, it was going to have to play on the Internet—and it would have to play by Net rules. It would have to accept the Internet standards—embrace them—and try to hold on to its kingpin position by extending them with Microsoft embellishments.

Microsoft shifted to Internet time, with the bombastic Ballmer beating the tempo. Recalls Gates: "Ballmer is saying, 'Well, where are we?' We're saying, 'Well, we have a lot of pieces, but it's not as comprehensive as it should be.' Ballmer is saying, 'Make it comprehensive, and have an event. In fact, pick a date, and you'll have it comprehensive by then.'"

Coming Attractions

INTERNET EXPLORER 3.0 A test version of Microsoft's latest Web browser is drawing raves. It ships in mid-August.

WINDOWS NT 4.0 An update to the "server" operating system, due in late summer, will have the Windows interface and free Web software.

"NORMANDY" NETWORKING SERVER A program for large-scale networks ships in early 1997.

INTERNET EXPLORER 4.0 At yearend, the browser will be merged with Windows and NT and will support Sun's Java.

OFFICE 97 WITH WEB LINKS The popular office suite gets Web-ized in late 1996.

"MERCHANT" ELECTRONIC COMMERCE SERVER Microsoft's server entry for setting up online stores on the Web ships at yearend.

The date was set: Paul A. Maritz, group vice-president for platforms would pull together an elaborate Internet summit for Dec. 7. Microsoft would announce plans for browsers, Web servers, and a new Web-based MSN—and other initiatives. Holed up in the boardroom, Maritz listened for two days as execs streamed through with their plans. Richard Tong, a Microsoft general manager, hit the road, picking the brains of Net consultants. Slivka's group wrote a 14-page memo on how Microsoft could get 30% of the browser market. It suggested getting AOL and CompuServe Inc. to license Microsoft's browser. **TRASH TALK.** At 8 p.m. on Dec. 6, Microsoft's top execs gathered at the Seattle Center auditorium for a dress rehearsal. They carefully went through each presentation. Gates even noodled with the language on the slides. (At the same time, executives from Microsoft and Sun were working through the night on a Java licensing agreement.) By midnight, the show was ready—until a PR exec told Gates the presentations were overwhelming. They needed a three-point summary for reporters. An exhausted Gates slumped to the floor, Ballmer next to him. Everyone waited, unsure if Gates was thinking or furious. Finally, he blurted out: "I just want them to get that we're hard-core about the Internet!"

*Glory, glory to the vision,
Though Netscape treats us with derision,
But soon will come the hour
When their stock price starts to sour,
We embrace and we extend!*

Since then, there has been no looking back. Microsoft employees tuned in to closed-circuit TV to hear the Internet briefing, got the speeches by E-mail, and later received videotape copies. Gates wanted it perfectly clear what the new marching orders were. He need not have worried, notes Chris Peters, vice-president of the Vermeer Product Unit. "If the chairman says success is defined as *that*, you will get a lot of *that*!"

Today, the Microsoft organization is pumped. "The thing that really motivates us is paranoia and competition," says Maritz. The day after Microsoft's Dec. 7 splash, Netscape CEO James L. Barksdale was asked about the threat Microsoft posed. His joking response: "God is on our side." That was like putting a match to dry kindling. "It's the kind of stuff that gets people up in a locker room," says Silverberg, who now heads Microsoft's Internet division. "I want to thank Netscape. All this trash talk helped get us motivated."



Microsoft is using more than school spirit. Within days of the summit, insiders say, it tried to buy Excite. The startup's "search-engine" technology, like that of its better-known rival Yahoo!, would help make MSN a useful gateway to the rest of the Web. Insiders say Microsoft offered \$75 million, but Excite turned it down after investment bankers said they could get more by going public. On Apr. 4, Excite went public and is now valued at \$84 million. Microsoft's next bid, an estimated \$130 million offer for Vermeer Technologies Inc., a startup with scant sales, succeeded. Vermeer's highly regarded FrontPage is used for creating Web pages.

On Feb. 12, Microsoft unveiled a key weapon in its contest with Netscape: the Internet Information Server. Some 90,000 free copies have been downloaded to date. March brought a major coup: From under the nose of Netscape, Microsoft snared a deal to have its Internet Explorer used as the primary Web browser on AOL. In exchange, Microsoft offered a big concession: putting AOL in Win95, ending an exclusive edge for MSN. Microsoft was on its way from Web wannabe to Web contender. Says Intel Corp. CEO Andrew S. Grove: "That was a masterpiece of pragmatic business attitude."

In June, Microsoft turned its attention to intranets—corporate networks built on Internet technology. On June 13, it lined an initiative centered on Windows NT 4.0, due late this summer. It will be crammed with Web features, including onPage and a new search program. That's attractive to firms such as Merrill Lynch & Co. that would prefer one super for conventional software and the newer Net applications. Microsoft is rolling out a trading system around 25,000 Windows PCs and 1,200 NT servers—with intranet and Internet connections. Bill Gates is counting on customers such as Merrill Lynch to stand by as his company fills in the remaining holes in Internet strategy. Microsoft still lags in programs for col-

laboration and electronic commerce, for instance.

The Net upstarts that goaded Microsoft say it's missing a lot more than a few pieces. They claim what's coming out of Redmond is mainly talk. "It doesn't take long to write an ad," sniffs Sun Microsystems CEO Scott G. McNealy. Gates says Microsoft is delivering what it has promised. But he also concedes his work is not done. "We're not saying we're out of the woods on this one," he says. "We have more than a year of incredible execution that we have to do." That's Internet time, mind you.

With Amy Cortese in New York and Rob Hof in San Mateo, Calif.

NETSCAPE: SITTING PRETTY—OR SITTING DUCK?

With Microsoft Corp. mobilized to create all sorts of Internet products and services, what's the view from Netscape Communications Corp.—the upstart whose lead in Net software helped rouse the sleeping giant? "They're working like all get-out, trying to take the food out of the mouths of my babies," says James L. Barksdale, Netscape's chief executive.

Nobody has yet missed a meal around Netscape's Mountain View (Calif.) headquarters. Despite Microsoft's parade of product announcements, acquisitions, and Web initiatives, Netscape still commands nearly 90% of the Web-browser business. Analysts figure the company's sales will more than triple, to \$250 million, this year.

Still, Microsoft's rise has clearly changed the atmosphere. Last summer, when it looked as if Netscape was walking away with the market, the startup's shares rocketed from an opening price of 28 to a staggering 171 (before a two-for-one split). Microsoft's shares, which had been stuck around 90, are up 40%, to 122, on the strength of Windows 95 and its increasing role in Internet software. After dropping by more than 50% in March, to around 40, Netscape's shares have climbed back to around 64, still more than 25% off their peak.

ALTERNATIVE. Whether the reversal in the stock market turns into a reversal in the software market remains to be seen. Netscape is promising all sorts of enhancements to Navigator that it says will not only keep it ahead of Microsoft but also produce a new soft-



NET GAME

Barksdale is rolling out a new version of Navigator in August

and Microsoft will relaunch Microsoft Network as a Web service—and showplace for its Net content and technology.

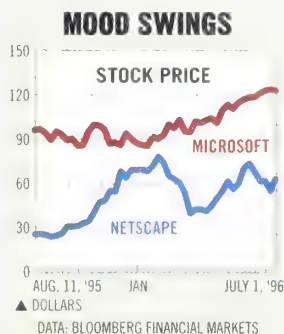
Microsoft's greatest resource, of course, is the leverage that Windows provides. It is the dominant software for desktop computers, and the industrial-strength Windows NT

version is becoming popular for corporate "network servers"—a key battleground for the Internet software market. Dataquest Inc. figures NT sales will triple, from 8 million this year to 24.4 million in 1997. Microsoft plans to load NT with all sorts of free Net software—from a Web server program to Web-site development "tools." If Microsoft can prove that it matches—or even approaches—Netscape in capabilities, as it is doing in browsers, that may be good enough to keep customers from switching to the newcomer.

Netscape, publicly, is unfazed. "The advantages Microsoft had in the past don't apply to the era of the network," says Barksdale.

Maybe not. But Microsoft, a global software empire with expected fiscal 1996 sales of \$8.6 billion and \$2 billion in aftertax profits, has one enduring edge. "One thing to remember about Microsoft," says Chairman William H. Gates III. "We don't need to make any revenue from Internet software." Who could forget?

By Robert D. Hof in Mountain View, Calif.



ware "platform" that is a clear alternative to Windows for Internet computing. A test version of Galileo, an update of Navigator that's due in September, lets users share documents, easily install add-on programs, and view more elaborate Web pages. And Netscape offers server programs tailored for specific Web businesses such as publishing and retailing. "They're turning around new products faster than anybody has ever seen," says Edward Glassman, director of technology strategy for Pfizer Inc., one of the dozens of major corporations building internal "intranets" with Navigator technology.

The next 18 months will be decisive. By yearend, every new Windows PC will come with Microsoft's Internet Explorer browser built into the operating system. America Online Inc. will offer Explorer free to its millions of customers,

NETWORK MEETS NET

How big an audience is there for Microsoft and NBC's cable-Web news venture?

Why would Microsoft Corp., happily cranking out profits in its core business, be willing to put up more than \$500 million to join NBC's plunge into the soon-to-be crowded cable news business? How could the software giant hope to see a payback, when ABC News scrapped a cable network rather than risk \$800 million getting caught in the coming brawl between the incumbent giant, CNN, and its challengers?

It's simple, says Patricia Q. Stonesifer, senior vice-president of Microsoft's Interactive Media Div.: "Microsoft has always tried to drive the number of dollars per PC." By investing heavily in multimedia CD-ROMs, for example, the company built up in a few years a new \$400 million-a-year business. Likewise, MSNBC, which will debut with much fanfare on July 15, has the potential to generate new revenue from PC owners by bringing together the promotional clout of a major network, a new cable channel, and a companion Web site. Online services, including interactive news, look like another winner, says Stonesifer.

Even so, Microsoft and NBC, a unit of General Electric Co., both concede that MSNBC is not likely to have an immediate payoff. Their goals are long-term. Microsoft hopes to build a bigger presence in the converging worlds of media and computers and expects that constant promotion on NBC and the MSNBC cable channel will drive consumers to the MSNBC Interactive Web site. If significant numbers of viewers are Net cruisers, too, the joint venture may prove the viability of an advertising-driven Internet site.

OVERSHADOW. For NBC, the MSNBC venture is a key step in expanding beyond its core U.S. broadcasting business. "For the future of NBC, this is the most important video service we're involved in," says NBC President Robert C. Wright. In 1986, when GE bought NBC, it had no non-broadcast assets and no international distribution. Since 1989, NBC has launched CNBC in the U.S., Europe, and Asia, an NBC channel in Asia, and NBC Super Channel in Europe. These properties now make up about 25% of NBC's asset base.

Ten years from now, NBC expects the value of its cable, international, and interactive assets to overshadow that of the U.S. broadcasting business. "MSNBC is not an appendage," says NBC Executive Vice-President Thomas Rogers, who, as the head of business development, negotiated the MSNBC partnership. "We're redefining what our core business is. This is the core business 10 years from now."

For both companies, the partnership is economically attractive. Last summer, Microsoft came close to investing \$1 billion in Turner Broadcasting System Inc. to create a similar venture with CNN. To get into the business



MIXED MEDIA Bill Gates and NBC's Bob Wright unveil plans for MSNBC

with NBC, whose audience for its nightly news program is 10 times as large as a typical CNN audience, Microsoft had only to invest \$220 million to buy a half-interest in NBC's America's Talking channel, which is being shut down and replaced by MSNBC. On top of that, Microsoft is paying NBC more than \$20 million a year in licensing fees for NBC news content that is used on MSNBC. It will also pay \$50 million annually for the next five years to fund its share of MSNBC day-to-day operations.

That adds up to about half what Microsoft might have spent with Turner. Still, says Pete Higgins, vice-president of Microsoft's Applications and Content Group. "It's our biggest outside investment." And he adds: "It's the cornerstone of our investment in interactive media."

NBC is getting an even better deal. Its \$50 million-a-year contribution to MSNBC through 2000 isn't much more than the \$30 million it had been spending to run America's Talking. Much of the content will be supplied by NBC, which spends about \$350 million a year on news operations to generate about \$100 million in profits. All told, with an annual budget of about \$100 million, MSNBC will be much cheaper to produce than CNN, which spends more than \$500 million annually on its newsgathering operation.

The MSNBC team has a key edge over other news startups in distribution. By taking over the America's Talking slot on cable systems, MSNBC will debut in 22 million homes





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and will pass a crucial threshold of 40 million in the next three years, Wright says. Rupert Murdoch's News Corp. expects to spend \$300 million, or \$10 per subscriber, to line up distribution to 30 million homes for its cable news channel, which debuts this fall.

What will MSNBC and MSNBC Interactive look like? The cable channel will offer all the slick promotional glitz and star power NBC News can muster. Tom Brokaw, Katie Couric, Jane Pauley, Bryant Gumbel, and Bill Moyers will anchor prime-time MSNBC fare, which will be a mix of interview, magazine, and news programs. Even with those big names, however, Wright is setting modest viewership goals. He says a "very successful" average rating in the next 18 months would be just 0.5—only 479,500 homes. *Larry King Live*, CNN's most popular show, averages a 1.2 rating. **BELLS AND WHISTLES.** The Web site will offer lots of interactive ways to go beyond the video programming. Peter Neupert, the Microsoft executive overseeing MSNBC Interactive, vows it will be "more than just a headline service." For one thing, MSNBC Interactive will offer a custom news service that will create a unique daily Web page for each consumer—with the news, weather, and even opinion that fit his or her preferences. It will also offer features to help interpret the news, such as a calculator to let PC owners figure out how a flat tax would affect them.

Executives on both sides quietly warn that on July 15 MSNBC, especially its Web site, may not have all the bells and whistles the hype might lead viewers to expect. The venture is being rushed out just seven months after being announced to catch big news events: the Olympics, the political conventions, and the Presidential election. Those events, coupled with a huge promotional campaign, will likely entice a large number of viewers to sample MSNBC both on cable and online.

The risk, warns Cowen & Co. media analyst Harold L. Vogel, is that viewers may be underwhelmed by what they see at first and not give MSNBC a second look. That's particularly true for the Web site, he says: "It's important for the interactive to be slick. People's attention has to be grabbed, and it has to stand out compared to other Web sites."

MSNBC's creators say they're not worried about any short-term glitches. Microsoft regards MSNBC as a strategic investment in Internet content. NBC is intent on adding ever more assets to set itself apart from its lagging network rivals. If MSNBC is a hit, it will put both companies, already leaders in their fields, even farther ahead of the pack.

By Elizabeth Lesly in New York and Kathy Rebello in Redmond, Wash.

The Corporation

TURNAROUNDS

IS IT RAINFOREST CRUNCH TIME?

To grow, Ben & Jerry's may have to trim its social agenda

Japan is beckoning to Ben & Jerry's Homemade Inc. While health-conscious Americans are swearing off superpremium ice cream, taking a bite out of Ben & Jerry's bottom line, the Japanese can't get enough: Last year, Häagen-Dazs raked in \$300 million there. So when a top Japanese supplier called Ben & Jerry's President and CEO Robert Holland Jr. to offer distribution, Holland might have jumped at the tasty deal. But after much board debate, he said no. Why? The Japanese company had no reputation for backing social causes. "The only clear reason to take the opportunity," says Holland, "was to make money."

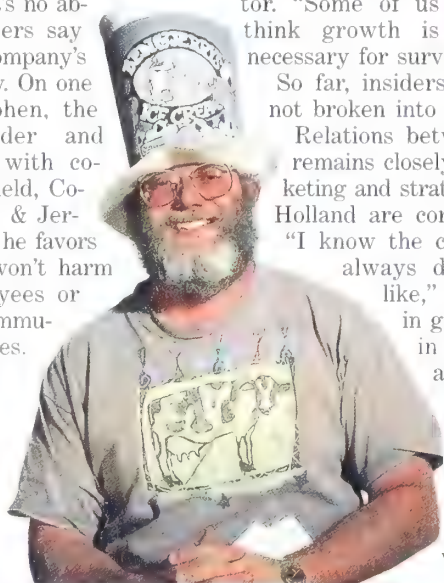
For most CEOs, that wouldn't have posed much of a dilemma. But the quirky Vermont ice-cream maker continues to operate by its own rules, even under Holland, a turnaround specialist and onetime McKinsey & Co. consultant who arrived 18 months ago to stop its earnings meltdown. By tightening operations, Holland has restored Ben & Jerry's finances. Now, as he expands into new products and foreign markets, Holland increasingly has to balance profits and social responsibility.

"BUDGET-SMUDGET." It's no abstract exercise. Insiders say a struggle over the company's direction is under way. On one side sits Ben R. Cohen, the charismatic co-founder and chairman. Together with co-founder Jerry Greenfield, Cohen owns 42% of Ben & Jerry's voting stock—and he favors slower growth that won't harm relations with employees or the tiny Vermont communities where it operates.

MISSIONARY
Cohen's vision
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launches linked
to social causes

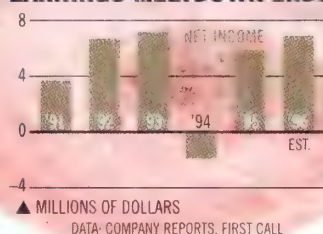
Pushing for swift-er growth are some members of the board, Holland, and a new team of professional managers from such mainstream companies as American Express Co. and The Limited Inc. Part of the pressure comes from shareholders—including Holland and other top executives, who now receive much compensation in options. But with the U.S. superpremium ice-cream market shrinking, Holland argues that Ben & Jerry's must expand its brand more aggressively or risk being frozen out of supermarkets. "It's not a fight over whether to grow but how fast," says one director. "Some of us think growth is necessary for survival."

So far, insiders say the rift has not broken into a power struggle. Relations between Cohen, who remains closely involved in marketing and strategic decisions, and Holland are cordial, if not close. "I know the company does not always do what I would like," says Cohen. "But in general, it's moving in a direction I'm aligned with." Board member and others say the debates are calm, not fractious. "Ben's not the kind of guy who says, 'If



"I get my way, I'm taking my toys home," adds Holland. Certainly, Holland has made lots of progress. In 1994, the ice-cream maker that had churned out a decade of double-digit earnings growth appeared broken. Struggling with cost overruns at a new plant, Cohen conceded the company had outgrown his management skills. As sales stagnated at about \$150 million in 1994, Ben & Jerry's lost nearly \$2 million. The once stock fell from a high of 33 to 10. With characteristic marketing flair, Cohen and Greenfield launched a gimmicky search for a CEO with a national essay contest. Great publicity

BEN & JERRY'S EARNINGS MELTDOWN ENDS



McKINSEY MAN

CEO Holland has brought a new fiscal discipline, made product development less haphazard, and pushed a line of popular sorbets

as sales hit \$155 million, earnings recovered to \$5.9 million. Shares now trade at 17. "We think it's an undervalued franchise," says one big shareholder.

Still, no one would call the ice-cream maker straight-laced. At 10 o'clock one recent morning, Ben and Jerry—who now

heads philanthropic efforts—roared into the parking lot on their new Harley-Davidson motorcycles. T-shirts and shorts remain standard attire, and Ben & Jerry's still gives three free pints a day to each of its 700 employees.

And Cohen's vision of "values-led" capitalism—in which returning something to customers, employees, and the community are as important as the bottom line—also maintains its sway. Ben & Jerry's pledges 7.5% of its pretax profits to social causes, from antinuclear campaigns to gay rights. It also uses purchasing power to back its values: It buys milk and cream from Vermont family farms, though that costs more, and buys organic fruits and nuts where possible.

Employees leave no doubt that the company today is more buttoned-down.

Holland, they say, is a more distant, traditional CEO. "It's less family-like," says Kendrick. Holland, adds one director, "brought adults to the company."

That has made for a sometimes rocky road. In employee surveys last year, staffers "questioned Ben & Jerry's commitment to its founding values as it grows." Many resent the board's decision to drop the salary cap that held executives to no more than seven times the lowest worker's pay. Holland's 1995 salary and bonus of \$326,000 is 14.5 times what an ice-cream scooper makes.

Yet the biggest stress may lie ahead. The new line of sorbets illustrates the trade-offs Ben & Jerry's confronts. The fruity line of six flavors has been a huge hit: In three months, Ben & Jerry's has grabbed a 25% share of the fast-growing, \$60 million premium sorbet category. The high-margined product is key to Ben & Jerry's improved bottom line and is driving sales growth.

Yet the company came to market a year behind Häagen-Dazs, delayed in part because sorbet held no clear link to its social mission. Profits—and a good opportunity to extend the brand—weren't enough. "Sorbets weren't high on Ben's agenda," says Director Henry Morgan. The obvious solution: use organic fruit. But so far, it hasn't found suppliers for big quantities. Since organic produce costs more than nonorganic, sorbet's juicy margins would also suffer. "BEACHED WHALE." And though Holland trumpets foreign markets as key to offsetting sluggish U.S. demand, progress has been slow. In part, that's because Ben & Jerry's lacked management depth. But its desire to expand only while exporting "caring capitalism" also hurt.

When the company prepared to launch in France last winter, for example, Cohen wanted to stay out of the market unless ads took a stand against the French government's policy of nuclear testing in the South Pacific. Holland resisted. "What are we gaining by not being there?" Holland asks. "If the decision is to punish French consumers because of their government's foreign policy, that didn't make sense."

In the end, Holland prevailed. But a compromise was struck to make the marketing campaign less splashy. Holland now regards the French launch as half-hearted. It's "either a beached whale or a pregnant cow," he says. "The market will be relatively small." Nor does Cohen appear satisfied. "I still believe it would have been the right thing to do," he says. "It also would have been, coincidentally, good marketing." As Ben & Jerry's continues to struggle with its growing pains, that's a debate the two are likely to continue.

By Paul C. Judge in Waterbury, Vt.

side, a corporate headhunter found Holland. He began by instituting tighter controls. For the first time, formal growth plans are being drawn up and budgets matter. "In the past, the feeling was 'budget-smudget,'" says sales manager Halsey Kendrick. "Now, people give numbers they're accountable for." Product development was equally haphazard: It often depended on what Cohen wanted to cook up. Now Holland has extended the research and development budget. And to end the manufacturing kinks, he hired an operations manager with years of experience in food service.

The changes have paid off. In June, Ben & Jerry's broke its record for week-end sales by 20%, thanks to the first fruits of Holland's labors: a new line of no-fat sorbets launched in March. Last year,

TIME TO BE WILD ABOUT HARRY?

CEO Stonecipher is revving things up at McDonnell Douglas

Outside the windows of the seventh-floor executive suite at McDonnell Douglas Corp., beneath echoing skies where fighter planes and carrier jets prove their mettle, looms a billboard that reveals just one of the hurdles facing CEO Harry C. Stonecipher. The St. Louis-based aerospace giant traditionally has rented the billboard to plug new aircraft and inspire pride and loyalty among workers. But in recent months, the space has often been hijacked by the company's union to trumpet some choice messages of its own. "Don't Be A Dirty Harry, Keep Our Jobs In St. Louis," one screamed. Demanded another: "Harry Stonecipher, Stop Outsourcing Our Jobs."

Since the 60-year-old Stonecipher took the helm nearly two years ago, he has had his share of successes—most notably, rescuing the troubled C-17 transport program. But he has also faced plenty of headaches. Two months after his arrival, Scandinavian Airlines System (SAS) bailed out of a gentleman's agreement to order the commercial airline division's proposed MD-95 and chose Boeing's 737 jetliner. A year later, Stonecipher bounced back with a commitment from ValuJet Airlines Inc. to buy 50 of the \$20 million, 100-seat planes. Late last year, secret talks with Boeing Co. about a possible merger of defense operations broke down. In early June, the union took its case beyond the billboard; 6,700 workers walked out. Then, on June 17, the Federal Aviation Administration

grounded ValuJet, leaving the only signed order for the MD-95 in limbo.

So far, though, Stonecipher hasn't buckled. The first nonfamily member to run the company, he has moved swiftly out of the shadow of his predecessor, John F. McDonnell. While McDonnell is still chairman, Stonecipher, who declined to be interviewed for this article, is putting his imprint on the \$14.3 billion



company—and stepping on some toes in the process. He has bruised egos by bringing in new managers, miffed workers by outsourcing jobs in the U.S. and abroad, and shaken up marketing by firing the old ad agency and hiring new salespeople. But his reforms have calmed a board that wanted more aggressive management. Since he took over, the stock price has moved from 18¢ to about 50¢, adjusted for two splits. In the first quarter of 1996, strong military performance pushed net earnings up 25% over a year earlier, to \$198 million. Says a board member: "Harry has even ex-

ceeded our high expectations. While he doesn't quite walk on water, he does know where all the rocks are."

Indeed, those rocks tripped up his predecessors. After founder James S. McDonnell retired in 1972, McDonnell Douglas suffered costly setbacks under his nephew, Sanford, and then his son John F., who took charge in 1988. Performance floundered in part because of an ill-fated \$1.5 billion investment in data processing, in part because the company ran so late and over budget on its contract to build the Air Force C-17 that by 1990, insolvency loomed. Before hiring Stonecipher, John McDonnell set the company back on course with a drastic restructuring that slashed operating costs and eliminated nearly half the workforce. But the C-17 program was still in trouble, and the commercial airline division, Douglas Aircraft Co., had been neglected. Today, Douglas shares of the world's jetliner market

STONECIPHER'S BUMPY RIDE

SEPTEMBER, 1994 Joins McDonnell Douglas as president and CEO.

NOVEMBER, 1994 Company loses a crucial SAS order for new 100-seat MD-95 jetliner

MAY, 1995 Wins \$14.2 billion contract to build 80 C-17 transports

OCTOBER, 1995 Bests Lockheed Martin for a \$1.5 billion contract to build "smart bombs"

DECEMBER, 1995 Negotiations with Boeing about combining their military operations collapse

JUNE, 1996 Nearly 6,700 workers strike over outsourcing, wages, and retiree health benefits

JUNE, 1996 FAA suspends operations of ValuJet, to date the sole customer for the MD-95

which stood at 22% in 1990, has fallen to 10%, vs. 60% for Boeing and 30% for Airbus Industrie.

Stonecipher is pushing hard to complete the turnaround. Decisive and hands-on, the son of a Tennessee coal miner started out as a lab technician at General Motors Corp.'s Allison Div. after earning a BS in physics from Tennessee Technological University. In 1960, he joined General Electric Co.'s jet-engine division, where he spent 27 years in engineering and management posts. In 1987, he moved to Sundstrand Corp. and within two years was named CEO, with a

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mandate to clean up the scandal-plagued aerospace and industrial parts maker. He negotiated a \$200 million settlement of charges that the company had overbilled the Pentagon. He also cut 4,100 of 13,600 jobs, yet Mel Paris, president of Sundstrand's Local 592, remembers him for reducing management-labor friction. Stonecipher didn't mince words or tolerate excuses, says Paris, but "he stopped on the plant floor to talk to people, and that impressed us."

At McDonnell Douglas, Stonecipher quickly scored victories on the defense side. He worked closely with the Pentagon to restore the C-17 program and in May, 1995, McDonnell won a \$14.2 billion contract to build 80 more of the cargo planes. In October, it won a \$1.5 billion Pentagon contract to build satellite-guided "smart bombs." And in June, the Air Force awarded McDonnell and Lockheed Martin Corp. a \$3 billion contract to develop a new missile system.

DESPERATE. Early on, Stonecipher decided the 29-year-old merger between McDonnell and Douglas had never been consummated. Some executives at Long Beach (Calif.)-based Douglas, for example, had never visited headquarters. So he set up task forces to foster the exchange of design, manufacturing, and management techniques. Among the early fruits: the discovery of technologies that can be used by both sides of the company.

The biggest challenges now lie in commercial aviation. One problem: Douglas, which accounts for about 27% of McDonnell's revenues, has relied on its 163-seat MD-90 and 300-passenger MD-11, rather than widen its array of planes as Boeing and Airbus have. Desperate to launch the smaller MD-95, Stonecipher is out hustling for Douglas. Early on, he began making overseas sales calls with the late Commerce Secretary Ronald H. Brown and leading his sales team in meetings to shore up relationships with customers in the U.S. and abroad. He dismissed J. Walter Thompson Co., McDonnell's agency for nearly 50 years, and hired McCann-Erickson Worldwide in a quest for ads that "make the hair on my arms stand up," according to Dan

O'Brien, who handled the account at Thompson. "He's shaking things up, so we had to go," says O'Brien, now with Ameritech. "And from the look of the new campaign, I think he has delivered."

"BRUTE FORCE." The executive suite bears Stonecipher's stamp, too. In May 1995, he lured Edward C. Bavaria, once a GE Engine marketing chief, out of retirement to help rebuild Douglas' customer base. And to wring out production inefficiencies, he recently made Michael M. Sears, who had managed some of McDonnell's most successful military pro-

grams, head of Douglas. Since Stonecipher arrived, Douglas' three-year product cycle time for new customers has been cut to 20 months. He's counting on Sears to drive it down further. "We haven't spent a lot of money on equipment and technology," notes Michael Marino, a manufacturing general manager. "A lot of the cycle time we cut with brute force."

Stonecipher has been less successful in the market. Douglas snared just 11 aircraft orders in the first quarter while Boeing won 180. Since ValuJet's grounding, Stonecipher has been pursuing officials of Northwest and Continental, which own

fleets of aging DC-9s the MD-95 would replace. "If ValuJet doesn't stay viable, there are plenty of other possibilities," says one McDonnell executive, who says company research indicates airlines will purchase between 1,700 and 2,000 planes in the 100-seat niche over the next 20 years.

It seems unlikely Stonecipher will pry himself off the hot seat soon. He's playing hardball with the union by hiring temporary replacement workers, and the strike could drag on, observers say, as the company exploits it to implement sweeping changes in its St. Louis plants. He's also standing firm on outsourcing.

Stonecipher never planned on a long honeymoon, anyway. Shortly after taking over, he told one executive: "For the first 100 days, I'm going to get along with everyone. After that, everybody's going to have to get along with me." And for those who don't, there's always the billboard.

By Ron Stodghill II in Chicago

IMPRINT
Stonecipher's reforms have calmed a restive McDonnell Douglas board. "While Harry doesn't quite walk on water, he does know where all the rocks are," says a director

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GOLF

THE LPGA COMES BLASTING DOWN THE FAIRWAY

How new commish Jim Ritts is pumping up the women's tour

The day Jim Ritts was named commissioner of the Ladies Professional Golf Assn., a dated photo in *USA Today* showed him with shoulder-length hair. The ex-Whittle Communications executive was an unknown in the golf world, and the long locks shocked some tournament sponsors. They were relieved when Ritts appeared for his first press conference with a corporate coiffure. "Half the room is thrilled my hair is considerably shorter," Ritts laughed. "And half is disappointed, and that's about the level of consensus we're probably going to have on most issues."

But there is considerable agreement among players, sponsors, and golf industry executives about the dynamic round Ritts is playing for the LPGA. While ex-Commissioner Charles S. Mechem Jr. is credited with bringing stability and professionalism to the organization, Ritts, 42, is capitalizing on that legacy by broadening its reach and adding marketing pizzazz—hoping to play off the popularity of golf and the increasing recognition of women athletes.

When Ritts took office in January, he aimed for 41 events with prize money totaling \$30 million by 1998. Already, three tournaments have been added this year and four to the 1997 schedule, bringing the total to 42 events. Purses will add up to \$29 million—within \$1 million of the goal and a year sooner than planned.

FRESH FACES. Luring sponsors, particularly those with what Ritts calls a "national agenda," is key. Companies such as State Farm Mutual, which has held the State Farm Rail Classic in Springfield, Ill., for three years, have renewed agreements, and new sponsors have signed on. Most notable is a five-year commitment from ITT Co. for a November tour-ending championship in Las Vegas to be aired on ABC.

This year, 29 LPGA events will be

televised, and Ritts wants to boost that to at least 33 by 1998, with a goal to have all events eventually on the tube. "Our ratings [on LPGA events] are getting stronger," says Jonathan D. Miller, senior vice-president at NBC Sports. "The LPGA tour is really one of the best opportunities for growth in all of golf." One potential audience booster: some of the 5.4 million

AHEAD OF SCHEDULE

Ritts has already almost passed his

goal of 41 events and \$30 million in prizes by '98

women who hit the links in 1995, a 20% increase in the space of a decade. LPGA ratings still lag behind women's tennis and men's golf overall, but Miller notes that

ratings for the U.S. Women's Open are holding steady in spite of an overall drop for golf—down 11% for all networks this year.

While several women were considered for commissioner, Ritts's media and marketing background won him the job. After becoming the youngest vice-president at New York ad agency Dancer Fitzgerald Sample Inc. at age 27, Ritts moved to Whittle Communications in 1984 as marketing director and co-founded its educational TV project, Channel One. A call from a headhunter and LPGA board member landed him in the race to be commissioner.

As the selection process was winding down, a firestorm of controversy arose over remarks by then-CBS women's golf commentator Ben Wright about a lesbian image hurting women's golf. While former Commissioner Mechem deflected the remarks, Ritts draws kudos from players and sponsors for his deft handling of the inevitable "anniversary" stories that appeared earlier this year. The intense coverage became "a fulcrum to examine the health of our business," he says. "Everyone put us under a real microscope, and this patient is not just surviving, this patient is extraordinarily healthy."

NO HYPE. Still, LPGA players have yet to achieve the name recognition of their counterparts in women's tennis or men's golf. One factor is that all Professional Golf Assn. events are televised, and major women's tennis events are teamed with men's. Building LPGA TV exposure will help. So will the growing use of women to promote golf equipment: Women's U.S. Open Champion Annika Sorenstam now pitches for Callaway Golf Co., and Dottie Pepper is a Titleist & Foot-Joy Worldwide spokesperson. While the LPGA will benefit from attention to top players, Ritts is wary of "manufacturing" superstars to sell the LPGA or overcommercializing the tour. "I like to experiment, and as I build a business, I like to tweak," he says. But "I'm going to have to be careful to temper my desire to experiment in dramatic ways with the measure of respect the game requires."

Not that he has much time for experiments yet. Ritts and his wife, Linda, have bought a housing plot in Daytona Beach, where the LPGA is headquartered, but ground has yet to be broken. Jim Ritts has a golf tour to build.

By Gail DeGeorge in Miami



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UNIONS

THE SAGINAW SOLUTION

GM and the UAW bend a bit—and a parts plant is reborn

Back in the early 1990s, General Motors Corp.'s steering-column plant in Saginaw, Mich., was a typical GM dinosaur. It used decades-old mass-production techniques in which each worker added parts to every column that rolled by. They complained of the numbing, repetitive nature of their jobs. Productivity growth was flat, reject levels were high. Most of the plant's output went to GM assembly plants, a captive market that put little pressure on Saginaw to improve.

Then, in 1993, with GM's parts operations hemorrhaging red ink and the implied threat of a sale hanging over Saginaw's head, plant managers and the United Auto Workers local agreed to join hands and fix their problems together. The process has been painful and is by no means complete. Yet today, Saginaw enjoys sharply rising productivity and even won a contract in 1995 from a Toyota Motor Corp. assembly plant in Georgetown, Ky. "I've always been critical of how GM makes parts, but Saginaw's quality has been impres-

sive," says Ronald E. Harbour, vice-president of Harbour & Associates Inc., an automotive consultant in Troy, Mich.

Saginaw holds important lessons for GM and the UAW as they continue labor talks under way since early June. A flash point in the bargaining over a new national labor pact is how to make Delphi, GM's sprawling components division, more competitive. GM says it must re-

WHY OUTSOURCE?

The UAW says that the lean production techniques and team approach used in Saginaw should be deployed at 12 other Delphi plants

tain the right to subcontract work to cheaper outside suppliers. Already, Delphi has sold 14 part units since 1992, and it recently announced plans to close or sell four more plants, threatening thousands of UAW jobs. Of the 5 Delphi plants represented by the UAW, a dozen are unprofitable, says GM parts chief J.T. Battenberg III. And the money-losers are at risk. "The key is to lose what you're not competitive in," Battenberg says. The problem is predominantly with GM, since

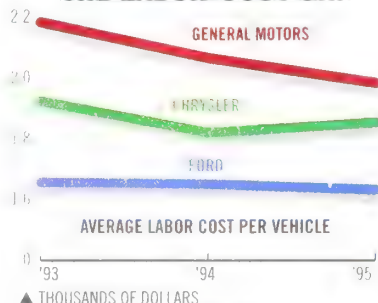
Ford Motor Co. and Chrysler Corp. already buy more parts from outsiders.

The UAW thinks GM is taking the easy way out. Only four years ago, say officials, Delphi had 50 troubled part plants. GM has restored half to profitability not by cutting pay but by adopting the Saginaw approach: streamlining production, giving workers more responsibility, and instituting lean manufacturing techniques. Indeed, GM's labor-cost gap with Ford and Chrysler continues to shrink, according to a new Harbour & Associates study (chart). Still, the union wants Delphi to take the same tack with the remaining dozen money-losers and is pushing for a ban on outsourcing in the new labor pact.

HANDY STICK. The problem is that both sides have a point. Delphi probably could fix many remaining problems and avoid most outsourcing. But the task is a difficult one that requires commitment, goodwill, and a degree of flexibility that has often been lacking in both camps. Meanwhile, GM doesn't want to get locked in, since it wishes to retain outsourcing as a stick with which to prod recalcitrant locals. "Historically, we have not done a good job of building trust," concedes Battenberg.

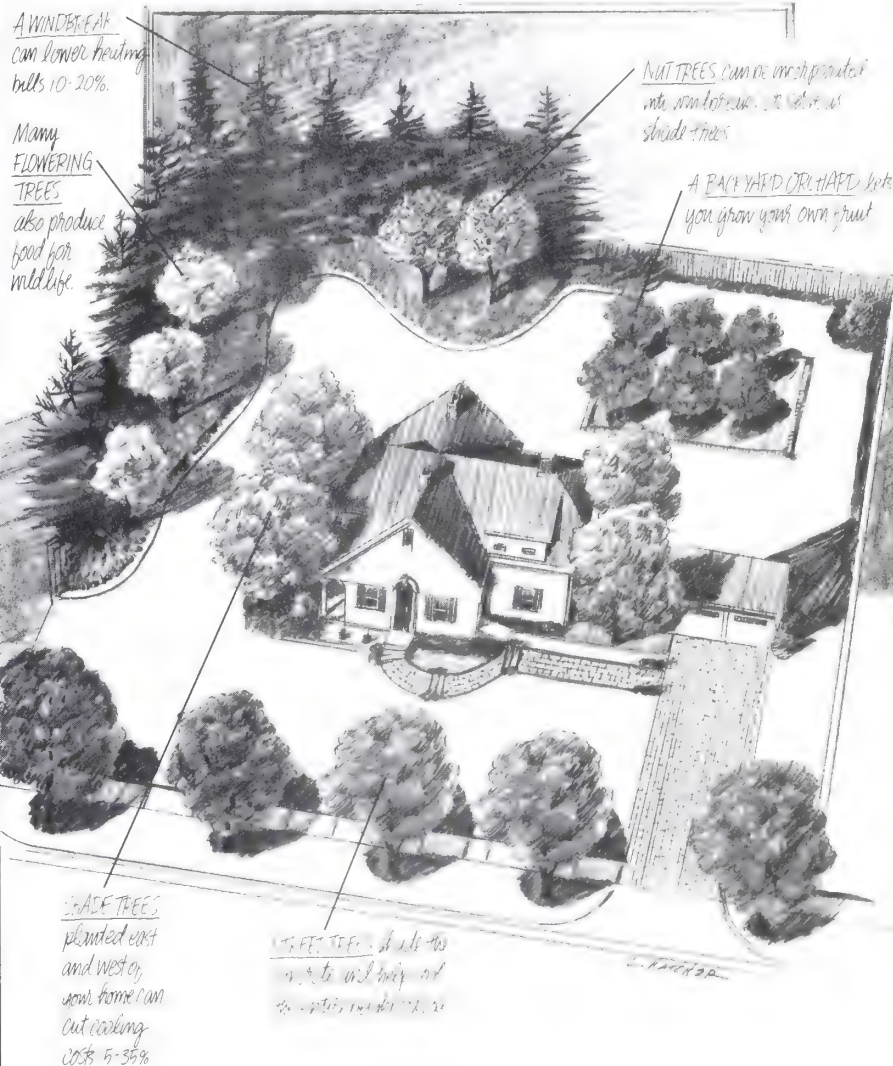
Saginaw shows how important that trust can be. After marathon talks and a contentious local election, the union penned a deal in 1993 that slashed job classifications from 160 to 12 and formed teams around specific steering products. It scrubbed job assignments based on seniority and agreed to rotate workers among jobs. Teams began to plan everything from production techniques to vacations. In return, GM pledged 40 hours

GM IS CLOSING THE LABOR-COST GAP



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additional training for all 2,000 work- and doled out raises of 29¢ an hour employees who agreed to job rotations. "We couldn't fight the company with and nail anymore," says Mike Ans, a 28-year veteran of the plant. The results have been dramatic. The new work methods have boosted morale and allowed workers to find more efficient ways of doing their jobs. Each production "cell" is autonomous and reves components already assembled in a nearby team, giving the groups unprecedented control over their work. Workers are also involved in the design of the unit, including the placement of machinery and the work station's ergonomics. All this helped to lift productivity by 14% last year. Quality defects are down 58%.

ANY HOLDOUTS. Still, Saginaw isn't where it should be. Even after three years, GM has failed to convert nearly a half of the workforce to lean manufacturing. Walk through the plant and you'll see yesterday and today side by side. In some spots, teams of eight or so work on machines set up around a common area, with each worker changing jobs every few hours. Some even have their own business cards for company-sponsored marketing trips to Toyota's Georgetown plant. Nearby, though, an additional assembly line still snakes through part of the building. GM has to spend the money to convert the old line and is loath to lose production during the changeover. "We still have a long ways to go," says Gary Shepherd, official at Saginaw's UAW Local 699. GM has had less success remaking her Delphi plants. Some are still plagued by combative labor relations, and GM is often quick to outsource. In fact, all 14 of the plants Delphi sold are reforming better and still supply GM. Battenberg concedes that Delphi lacked the management depth to fix some plants. He also argues that it was a matter of priorities. "Could we have mended these 14 businesses around?" asks Battenberg. "Probably, yes. But there wasn't enough money, so something else would have suffered." In recent months, Saginaw has become something of a showcase for GM and the UAW alike. Battenberg has urged the plant with Vice-Chairman Larry J. Pearce and influential GM Director John G. Smale. And leaders of a dozen or so other UAW locals have ekked up to the complex about 80 miles north of Detroit. The lesson is clear: Change is difficult, but it's possible, even at a strife-ridden company such as GM. The question is whether both sides will remember that message when their pact expires in September.

By Bill Vlasic in Detroit

TOO MUCH ON BOB BASS'S PLATE?

Specialty Foods looked like a tasty dish. Now Bass wants to unload it—and that may prove difficult

When billionaire dealmaker Robert M. Bass and his partners got a hankering for the food business three years ago, they dusted off a familiar recipe: find an undermanaged company, sprinkle a few crumbs of equity into a stew of debt, and *voilà*—a classic 1980s-style leveraged buyout. At \$1.1 billion, their LBO of Specialty Foods Corp. was the biggest of 1993. It brought the top-shelf dealmakers businesses making everything from bread and sausage to kosher pickles—and a chance to turn low-rent brands into money machines.

But instead of savoring an easy payoff, the Texas mogul and his investors are trying to get out from under the deal. Applying the storied LBO formula a bit too liberally, Bass larded the company with excessive debt. Now, as he moves to bust up the food conglomerate, which has \$2 billion in sales, his exit strategy looks risky. A handful of operating units he put on the block in June might fetch less than the rich multiples of cash flow that he and his partners hope for. And a plan to sell or spin off the remaining bread and cheese businesses within a few years depends heavily on a big drop in commodity prices—hardly a sure bet. In the meantime, debt service is siphoning off returns and handcuffing growth.

Specialty Food executives predict those challenges will be overcome.

"There is a home plate in sight, and we're in scoring position," says Robert B. Haas, the Bass-backed investment banker who serves as the company's chairman. Yet the equity investors, led by Bass-controlled Keystone Inc. and Acadia Partners LP, may wind up with little to show for their \$125 million cash investment. While loans from Chemical Bank are secured by company assets and senior debt holders have little to fear from the bust-up plan, Specialty's least-senior junk debt trades at a steep discount. "It's not a company that's free and clear. It's dicey as to how much they can recover," says Thomas N. Haag, manager of the \$700 million Lutheran Brotherhood High-Yield fund, which recently sold Specialty's subordinated debt in favor of its senior securities. The market values that subordinated debt at about 65¢ on the dollar.

UNDISCOVERED GEM. Companies have had a field day buying businesses in their industries with stock buoyed by the bull market. They can then generate economies of scale by integrating new operations into their own. But LBO players don't have a ready-made acquisition currency, nor do they come to the table with existing operations in the same business. They use leverage and run the risk of overpaying—as in the case of Specialty, which wrote down one-third of its goodwill at yearend. It now expects to sell off some of its divisions, probably to companies in the same business. "There are strategic buyers out there that can do more with these businesses than we can," says Paul J. Liska, who became Specialty's chief executive in January.

Back in 1993, the Bass group thought



it had found an undiscovered gem in Specialty Foods. The company had virtually no public profile. The seller, Belgian holding company Artal, had cobbled together a large hodgepodge of U.S. food businesses in the previous decade. Artal initially sought to sell only a single unit, Metz Baking Co., but the Bass group persuaded Artal to sell all eight of its food businesses.

At the outset, Specialty's parent seemed to offer it every advantage. The veteran Haas, of Haas Wheat & Partners in Dallas, pulled off the deal's financing without a hitch, in spite of debt

Saga of an Ailing LBO

AUG. 16, 1993

Investment group led by Robert M. Bass buys Specialty Foods Corp. Its eight businesses include cheesemaker Stella Foods, breadmaker

Metz Baking, and sausage-maker H&M Food Systems.

DEC. 1, 1993

New management team led by former Kraft exec Thomas

Herskovits begins to cut costs and beef up marketing. Operating woes emerge in cheese and meats.

APR. 5, 1995

Citing competitive

market, Moody's Investors Service downgrades three Specialty bond issues. Poor pricing environment makes company vulnerable to commodity price swings.

The 1993 deal followed the classic LBO recipe—but the company isn't growing fast enough to accommodate its enormous debt. Even selling off star performer Mother's Cake & Cookie may not bring a huge payday



CEO LISKA (LEFT) NEEDS TO BUILD UP THE BREAD AND CHEESE BUSINESSES FOR BASS TO SEE ANY RETURN ON HIS INVESTMENT

ating units and worked feverishly to integrate businesses. Specialty's \$750 million Stella Foods Inc. cheese unit, for instance, had five separate sales forces, managements, and ledgers.

Yet from the beginning, one operating woe or another undermined the company's growth. First, the cheese business ran into trouble. Its management had difficulty coordinating milk purchases while trying to combine its various businesses. As well, an across-the-board price increase alienated customers and hurt top-line growth.

Problems then emerged at H&M Food Systems Co., which makes precooked meat products such as sausage for restaurant chains and food manufacturers. Early in 1995,

a competitor lured away H&M's biggest customer, Pizza Hut. Meanwhile, falling meat prices hurt profits. H&M's contracts with customers allow it to recover only its costs plus a fixed percentage markup. So in a falling market, the dollar markup is less.

As meat prices fell, grain prices soared, damaging the bakery units. In addition to Metz Bakery, the company owns Mother's Cake & Cookie Co. Metz markets brands such as Healthy Choice and Taystee breads. Competition was taking its toll: In-store bakeries were making fresher products. And overcapacity gave the upper hand to companies with greater flexibility and lower fixed costs.

By the end of 1995, it was obvious that Specialty Foods would miss its sales and earnings targets by a mile. While its cash flow had expanded by some \$30 million since 1993, to \$157 million, sales had been roughly flat at \$2 billion. An operating profit of \$83

million in 1994 gave way to a 1995 loss of \$165 million as the company wrote down goodwill.

In the wake of such results, Herskovits stepped down on Jan. 12. He was replaced by Liska, another Kraft alumnus who had joined the company as chief financial officer soon after the buyout.

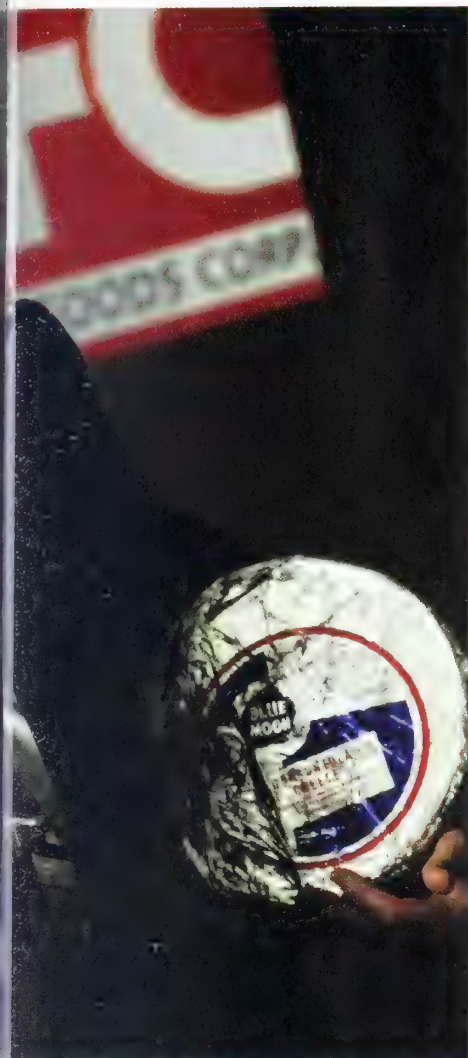
Liska has his work cut out for him. Granted, the company now has a lower cost structure, higher-caliber management, and better marketing. But in a 10-Q filing on May 14, Liska warned that the company's cash flow might be insufficient to meet debt obligations and that credit covenants could be violated if business conditions didn't improve.

TOUGH MARKETS. On June 6, Merrill Lynch & Co. put Specialty's smaller holdings up for sale. Liska says the response has been "overwhelming." But H&M remains troubled. And even the most attractive property for sale, Mother's Cake & Cookie, won't bring a huge payoff, predicts analyst Kevin A. Eng of Grantchester Securities, the high-yield arm of Wasserstein Perella Securities Inc.: "There is nothing that commands a premium."

The remaining bread and cheese businesses offer some promise for Bass and his investors. By taking big writedowns, Specialty has set up those units to show better results. It is hoping to beef them up with add-on acquisitions financed with some of the proceeds from the planned asset sales. Then, if commodity prices reverse, the bread and cheese businesses could become candidates for initial public offerings or sales.

For now, though, Specialty must grapple with tough markets and intense competitive pressure. Gobbling up Specialty Foods was no problem for the dealmakers surrounding Bass. Spitting it out is another story.

By Greg Burns in Chicago



es exceeding eight times cash flow. carry out an aggressive cost-cutting in and jump-start undermarketed inds, the company paid top dollar for gh-powered executives. Half a dozen ne from Kraft Foods Inc., the nann's largest food company, including mer Specialty Foods Chief Executive Thomas Herskovits, a powerhouse io had headed Kraft's dairy and zen-food operations.

By early 1994, Herskovits was inlled as CEO and Specialty was primed a cost-cutting spree. The company t rid of middle managers at the oper-

l, 1995

ces soar, meat unge. Company wn \$253 mil- odwill, citing nt cash flow in d meats. Her- signs Jan. 12.

JUNE 6, 1996

Merrill Lynch & Co. is hired to sell noncore holdings. Company retains bread and cheese businesses for a sale once commodity prices improve.

COMMENTARY

By Jeffrey M. Laderman

ARE STOCKS OVERPRICED—OR THE YARDSTICKS FLAWED?

If you look at conventional stock market ratios and listen to the gurus who follow them, stocks are about to tumble into the abyss. The market's price-earnings ratio is above its long-term average; the dividend yield, well below. Then there's the "Q ratio," which compares corporations' market value with the replacement cost of their physical and financial assets. The Q ratio says the market is 70% overpriced. Conclusions: If you own stocks, get out. If you're thinking of investing, wait.

It's tempting to latch on to such pronouncements, especially since stocks have risen more than 50% in the past 20 months. And these indicators distill a lot of data into easily digestible capsules. But wait: As predictors, they're seriously flawed. Relying on them is akin to driving with your eyes fixed on the rearview mirror.

The indicator generating the most interest these days is the Q. This ratio, developed three decades ago by James Tobin, 1981 Nobel laureate in economics, compares the total market value of the nation's stocks and bonds with what it would cost to replace all the corporations' assets. When the ratio is below 1.0, stocks are a buy, because it's cheaper to buy businesses than build them. But when the ratio is above 1.0—and it's now a historically high 1.7—stocks are overpriced. It's cheaper to build than buy.

INTANGIBLES. The problem is that the Q belongs more to the manufacturing economy of the 1960s than the service and information economy of today. Back then, the value of a company was largely its tangible assets, such as plant and equipment. Today, intangibles—human capital and brand names—count for a lot more. Take Microsoft Corp. Most of its value lies in its software products, its programmers, and its lead position in desktop computing, not in factories or offices. The stock, now at \$121, sells at nearly 11 times book value, which is reasonably close to the replacement cost of its tangible assets. So using a Q

analysis, Microsoft would be worth only \$11 a share.

Even when it comes to industrial companies, the Q misses the mark. "There's investment in computer software and worker training, which increase productivity but are expensed and don't show up on the balance sheet," says Abby Joseph Cohen, an investment strategist at Goldman, Sachs & Co. "Just because things don't fit nicely into our ac-

flation. According to Goldman Sachs figures, p-e ratios have, since 1950, averaged 16.2 during periods when inflation was below 3.5%.

More important, earnings growth is well above the long-term norm. From 1945 to 1995, S&P 500 earnings grew at 7.4% a year—or 3.1% after inflation. In the '90s, earnings growth is 9.7%—a striking 6.3% after inflation. Plus, the quality of earnings is better. Managements are more focused and are running leaner operations. Think of today's overall market as a high-quality growth stock. It deserves a higher-than-average p-e.

NOT FAIL-SAFE. Perhaps most irrelevant of the valuation indicators is the S&P dividend yield. The old saw: Stocks are overvalued when the yield falls below 3%. Well, that happened 4½ years ago—and the market is up by more than 60% since. Why don't dividends matter anymore?

Dividends are an inefficient way to reward shareholders. Tax rates are as high as 39.6%, and taxes are inescapable. Many companies prefer share repurchases. That usually boosts the stock, and the only investors who get hit with taxes are those who sell. Even then, they pay at the favorable capital-gains rate.

The fact that shareholders are ignoring dividends is not a cause for concern. It's a vote of confidence that corporate managements will use their cash to better purposes—buying in shares, paying down debt, or expanding the business.

Because these measures aren't appropriate for this market doesn't mean stocks won't sell off. A recession or an external shock, such as the fall of the Saudi ruling family, would send stocks reeling. But in such cases, you wouldn't get any advanced warning from the Q, the p-e, or dividend yields.

Senior writer Laderman watches the Ps and Qs of the stock market.



The "Q ratio,"
comparing the
market's total value
with total asset value,
is a Rust Belt relic

counting system doesn't mean they don't exist."

At first glance, the p-e ratio also suggests that the market is overvalued. The Standard & Poor's 500-stock index, now at 674, divided by the current year's forecast earnings, about \$40, gives an overall p-e of 16.9. But the average for the 1950-95 period is 14: Ergo, the market is overpriced—by 20%.

But averages can be misleading: They work only in an "average" environment. Actually, the market is enjoying a better-than-average backdrop of moderate growth and low in-

ALSA FOR NEW ENGLAND BANK

First National of Boston is hot in Latin America

Banking in Latin America is not for the fainthearted. Since 1995, more than 40 Brazilian institutions have led or merged, unable to adapt to the new low-inflation environment. In Argentina, 40 banks have folded or were forced to merge as panicky depositors withdrew \$8 billion last year in the wake of Mexico's financial crisis. Most foreign banks, unwilling to jump the region's economic roller coaster, have stayed away.

But First National Bank of Boston is enjoying the ride. Boston, the 18th-largest U.S. bank—with \$47 billion in assets—has made Latin America the center of its global expansion efforts. Operating profits rose 50% in the region last year, compared with 25% for the bank as a whole.

Brazil and Argentina, which account for 85% of the bank's Latin American revenues, economic reforms promise even better profit growth ahead.

As Latin America's large economies try to impose stability on inflation and change rates, a burgeoning middle class is turning to banks for new investment products and services. So Boston is moving aggressively into mutual funds, private banking, and credit cards and is targeting the potentially huge market for pension-fund management. "In terms of growth for a long period of time, [Latin America] could be one of our best areas," says William Shea, Boston's chief financial officer and head of international operations.

NEW PUSH. Shea's optimism is tempered by realism born of years of experience in the region. "From time to time there will be what the markets call crisis," says Henrique Meirelles, president of Boston's Brazil branch. For example, if a currency devaluation were followed by massive capital flight, Boston might have to abandon its push into consumer credit and home mortgage loans.

Still, the bank is about to rev up growth in the region. After Boston's \$2



billion acquisition of New England's BayBanks Inc., expected to close this month, non-U.S. operations will shrink from 21% to 12% of the new bank's total revenues. But Shea believes that non-U.S. business should account for 25% to 30% over the next several years. Says Gerard S. Cassidy, senior vice-president at Hancock Institutional Equity Services: "This gives Bank of Boston management down in Latin America a tremendous opportunity. They have never been



CFO SHEA

"In terms of growth for a long period of time, [Latin America] could be one of our best areas"

in full-speed-ahead mode before."

Ever since it followed New England wool traders to Argentina in 1917, Boston has made South America its specialty. When Argentina and Brazil began outlining stability programs in the early 1990s, Boston had already built a solid presence. With more than \$4 billion in assets in its Brazilian and Argentine operations, it has little competition from non-Latin banks in the region. Only Citibank directly challenges Boston throughout Latin America.

BOSTON'S BUENOS AIRES OFFICE: THE BANK HAS BEEN IN ARGENTINA SINCE 1917

The bank is pushing new products. In Argentina, where banks were allowed to enter the mutual-fund business only last year,

Boston is No. 1, with \$1 billion, or 30% of the market. Through an aggressive marketing effort, it has doubled its mutual-fund volume in Brazil since early 1995, to \$3.5 billion. Boston now issues nearly 350,000 credit cards, including United Airlines Mileage Plus cards, in the two countries—a 300% increase from 1994. The card business is modestly profitable so far.

Pension funds are the bank's next play. In Argentina, it is a partner with American International Group Inc. in a fund managing \$360 million. It's forming a fund with partners in Uruguay, which will soon open its pension system to investors. And although Brazil is years away from following suit, Boston is itching to get into that huge market.

FIRE SALES. The bank is also moving to expand its franchise to northern Latin America. It has opened branches in Mexico and Colombia in the past two years and will open one in Peru this year.

The bank wants to broaden its customer base by buying some of the troubled banks that litter Latin America's financial landscape. Although the bank would not confirm its interest in specific institutions, it's believed to be studying the purchase of a midsize retail bank, Banco Mexicano. Boston is also considered a contender to buy Brazilian Banco Meridional do Brasil.

Its volatile economies make the region a tricky ride. Meirelles is already bracing for Brazil to speed up its devaluation of the real within the next year. He doesn't foresee a Mexico-type collapse but expects some investors to run scared. "Stability in Latin America is a long-term movement," he says. "There will be setbacks." But when you see them coming, as Boston seems to, they're not so scary.

By Ian Katz in São Paulo, with Alison Rea and Joan Warner in New York

BY GENE G. MARCIAL

NO PREMIUM TO PAY FOR ALLMERICA

When a big insurer—then named State Mutual Life Assurance Co. of America—went public last October, selling 12 million shares at \$21 apiece, it also distributed 37.5 million shares free to its policyholders. Some 30 million of the shares in policyholders' hands have not yet been unloaded. This "overhang," say some market watchers, is depressing the stock price unduly and may be scaring away potential buyers.

But that hasn't stopped investment

MAYBE UNDULY DEPRESSED



manager Ed Wachenheim from snapping up shares of what's now called Allmerica Financial (AFC), trading on the Big Board at 29%.

Wachenheim, chairman and CEO of investment firm Greenhaven Associates in Purchase, N. Y., thinks that worry about the overhang—now down from 75% of the stock outstanding to 60%—has created a buying opportunity, even if all of the new owners eventually sell. Allmerica is "underfollowed and not well understood" on the Street, he says. That won't last long: Already, Fidelity Management has acquired a 7.5% stake.

Says Wachenheim: "In 6 to 12 months, most policyholders will have sold, and the overhang will be eliminated"—and that should drive up the price. Wachenheim figures the company, which owns 60% of Allmerica Property & Casualty, a major provider of auto and homeowner policies, will make more money this year and next than the Street expects.

He thinks Allmerica will earn \$3 a share in 1996 and \$3.40 in 1997, vs. analysts' consensus estimates of \$2.67

and \$3.08. Wachenheim reckons the stock is worth as much as 13 times his 1997 estimate, or 52 a share.

The earnings gains, he figures, will come from growing demand for its financial services, which include variable life insurance and managing retirement and health plans. Cost reductions and repurchase of its own shares will also augment net income, he adds. Wachenheim notes that Allmerica's book value, currently close to \$30 a share, should rise to \$33 or so in mid-1997 and to \$36 by mid-1998.

Analyst Thomas Cholnoky of Goldman Sachs, one of the underwriters of the public offering, says part of Allmerica's success hinges on its ability to expand "worksites marketing": offering group-rate plans for products such as auto insurance, 24-hour managed health care, and 401(k) plans.

STANDING TALL IN THE CHIP SLUMP?

Semiconductor shares have been under such heavy pressure that some investors think they're ripe for recovery. But instead of putting his money on memory-chip makers, money manager Scott Black is betting on KLA Instruments (KLAC), the world's leading maker of equipment and process-monitoring systems to test chips' quality and yield.

Despite concerns about overcapacity in semiconductors, Black, president of Delphi Management, thinks KLA is in a good position to weather turbulence in capital spending in computers and chips. He thinks such worries are already reflected in KLA's stock price, which dropped from 48 last September to 23 on July 1.

The company is flush with cash, has practically no debt, and has a book value of about \$10 a share. Says Black: "There's no question that this dominant player has hit a very attractive level." He figures that the increasing cash flow and a steady order backlog will bolster the results this year and next and that the stock will double in 12 months.

Black expects earnings to jump to \$2.60 a share for the year ending June 30, 1997, up from an estimated \$2.35 for fiscal 1996 and \$1.53 in 1995. The Street's consensus for 1997 earnings is even higher—\$2.76, according to Zacks Investment Research.

A big boost to earnings, says Black,

will come from Korean chipmakers. He thinks they'll hold down production of 16K dynamic random-access memories and switch to more powerful 64K DRAMS. When this happens, says Black, the demand for KLA's services will rev up. If computers start using the new 64K DRAMS, "it will be an entirely new—and bigger—ballgame for KLA," Black says, as chipmakers will need new and even more efficient testing of the new chips.

BANANAS OVER DOLE FOOD

Gerry Sullivan is no trader, but he sometimes acts like one. He runs a growth-and-income fund at SunAmerica Asset Management, which manages some \$2.1 billion. Sullivan patiently looks for quick-changing patterns or price pullbacks before buying.

Take Dole Food (DOL). Sullivan seized an opportunity to buy when shares slumped to 34 early in January. And he continued to buy even though the stock was going up—to 43 by July 1. What's on Dole's plate? Bananas and pre-cut vegetable salads.

Sullivan, whose SunAmerica Growth & Income Fund has racked up a gain of 35% in the past 12 months, insists Dole is undervalued. Its top moneymakers are bananas, which pull in 35% of earnings, and salad veggies, 20%. "Demand for these two items is strong," says Sullivan, who thinks earnings will hit \$3.30 a share for 1997 vs. \$2.50 for 1996 and \$1.55 last year.

Sullivan thinks the stock will rise above 50 as Dole gains better Street following. Indeed, it perked up in December (after several years of depression), when the company split in two, with Castle & Cooke taking most of the real estate. Sullivan thinks Dole hasn't finished selling assets—such as properties in countries where bad weather frequently interferes with growing crops. He says Dole wants to buy a greater share of the produce it needs.

PERKING UP AFTER A SPLIT-UP





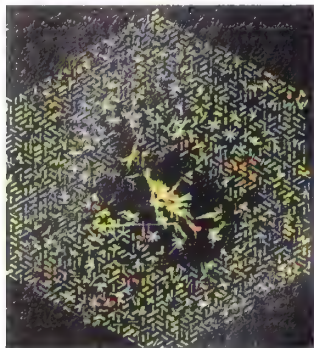
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SOON, MARKETERS MAY 'VISUALIZE' YOUR PHONE CALLS

PHONE COMPANIES ARE SITTING on gold mines of information. Details about who calls whom, how long they're on the phone, and whether a line is used for fax as well as voice can be invaluable in targeting sales of services and equipment to specific customers. But these tidbits are buried under masses of unintelligible numbers.

AT&T's equipment spin-off, Lucent Technologies Inc., is using "data visualization" to bring information to life. Instead of people trying to extract meaning from columns of endless digits, a computer converts the numbers into graphics that can unmask previously hidden patterns. For example, each line in the illustration above is a call between dots, or phones. Note the island at the center. This marks a cluster of heavy callers who talked to one another a lot. Yet they made few outside calls.

The software can peel away low-volume callers, find the people who account for most calls, or display only calls that lasted more than an hour. Many marketing programs could be fine-tuned with the use of such information, says Daniel E. Fyock, technical manager in Lucent's data-visualization products group. *Peter Coy*

DOING ULTRAVIOLENCE TO PARASITES

ENGINEERS HAVE USED ULTRAVIOLET LIGHT TO ZAP BACTERIA in industrial wastewater for a decade. The process is expensive, though, and it doesn't kill some hardy parasites such as *cryptosporidium* and *giardia*. So UV technology has yet to be used for treating drinking water. But one day, it could be—thus ending the need to lace tap water with chlorine.

Safe Water Solutions in Milwaukee, a joint venture between two pollution-control-equipment makers, one British and one American, has developed a UV-based system now under evaluation by the American Waste Water Assn. The key is a superfine filter that collects the parasites and exposes them to a longer dose of UV light than they would receive simply by flowing in water under the light source.

Another potential solution is being developed by Los Alamos National Laboratory and Triton Thalassic Technologies Inc. in Ridgefield, Conn. Los Alamos created a special lamp that emits just one narrow segment of the UV light spectrum. This not only saves energy, says the chairman of Triton Thalassic, Barry Ressler, but also improves bug-zapping power tenfold by concentrating the UV output in a highly lethal band.

Initially, the company hopes to sell its system to manufacturers as an alternative to the toxic chemicals used today to kill microbes in industrial fluids. After that, Thalassic may try to tackle drinking water. *Greg Greenberg*



INNOVATIONS

■ Expiration dates on packages of perishable foods may soon expire themselves. Life Lines Technology in Morris Plains, N.J., has developed "smart" labels that change color to indicate when the food may have gone bad. The label keeps tabs on the temperatures to which the package is exposed. If a frozen food package, for example, sits unrefrigerated for long, the label would signal consumers—even though a calendar expiration date might be weeks away.

■ Australian couples who want to divorce without going to court can ask an unemotional computer for suggestions about how their marital assets ought to be divided up. The allocations are determined by Split Up, savvy software developed by researchers at La Trobe University. The program also explains its recommendations.

■ Move over, melatonin. Scientists at Scripps Research Institute in La Jolla, Calif., are experimenting with compounds that prevent the body from getting rid of oleamide. That's the chemical that induces sleep. The potion is now being tested with mice.

FILL 'ER UP—WITH SUGAR AND ENZYMES

POUR SUGAR INTO A CAR'S gasoline tank today, and it's sure to gum up the works. But tomorrow, dumping sugar into the gas tank may be just the ticket for cleaner air and cheaper fuel. Sugars and starches, from glucose and dextrose down to the cellulose in grass mowings and other plant waste, would be converted into hydrogen, perhaps the

least polluting fuel of all.

The secret to this magical transformation: two deep-sea enzymes. They come from bacteria that live near the volcanic vents in the deepest, darkest abysses of the sea. Unlike enzymes that evolved under normal conditions, the new enzymes have unusual properties. For example, one of them can donate an electron to a chemi-

cal reaction. As a result, the enzyme pair can pluck atoms from glucose molecules and reassemble them into hydrogen molecules.

If the process can be scaled up, "we could obtain large volumes of hydrogen fuel from renewable resources," says Jonathan Woodward, a researcher at Oak Ridge National Laboratory. He works with biochemist Michael Danson at Britain's University of Bath. □

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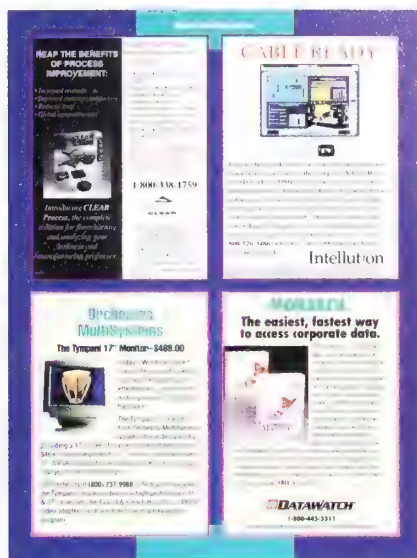
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STAR WARS JUNIOR: WILL IT FLY?

Although kinks remain, a new antimissile system may be workable—and expensive

At 5 a.m. on Dec. 13, a white, pencil-thin missile lifted off flawlessly from a mobile launcher into the starry skies above White Sands Missile Range in New Mexico. The Theater High-Altitude Area Defense (THAAD) payload separated from its booster stage, shed the shrouds protecting its super-sensitive infrared sensor, and locked on target—a dummy ballistic missile. Then...bust. A software glitch sent the THAAD in the wrong direction. The 20-foot-long missile corrected course, but too late. Before it could intercept and kill the target, the THAAD ran out of fuel.

The encouraging launch and its disappointing outcome provide an apt metaphor for the current state of the nation's ballistic-missile defense program. Many of the program's new gizmos work well. The Pentagon has made great strides in technology, from new thruster systems to MADCAP data-processing techniques. (It stands for "mosaic array data compression and processing.") But the experts haven't worked out all the kinks in missile defense. "It's an extremely difficult technical problem," says U.S. Air Force Secretary Sheila E. Widnall.

ROGUE NUKES. It's a tricky political problem, too, now that former Senator Bob Dole wants to make the development of a scaled-back Star Wars system a cornerstone of his Presidential campaign. THAAD, a system designed to protect troops from short-range missiles in a war theater, is a junior version of the big kahuna Dole wants: a scheme to protect the entire U.S. from intercontinental ballistic missiles. Spurred by focus groups of voters who are shocked to learn the U.S. has no defensive umbrella against a nuclear attack, Republicans hope to use the issue to make President Clinton look weak on defense. Democrats agree that there's a long-term threat and a need for such a system. But they want to focus spending now on the less ambitious goal of protecting soldiers and sailors from at-

tacks by short-range, Scud-like missiles.

Beyond the question of what Washington should do is the question of what the U.S. is able to do. Unlike Ronald Reagan's Star Wars vision of a shield against thousands of incoming Soviet missiles, which may be technologically impossible, the goal of a national missile defense today is to thwart a handful of nukes launched by a rogue state such as North Korea or Iran. The Congressional Budget Office estimates the Pentagon plan for such a limited missile defense would cost \$6 billion over the next five years. Even opponents agree the Pentagon plan is feasible. "I don't see any

SPOTTING THE INCOMING

Ground-based radars and space-based infrared sensors on satellites in high and low orbits scan the skies for incoming missiles.

reason why they shouldn't eventually be able to hit targets," says critic Theodore Postol, professor of science, technology, and national security policy at Massachusetts Institute of Technology.

Any national system would be far more sophisticated than past programs, such as Sentinel and Safeguard, that relied on nuclear-tipped warheads to obliterate anything that threatened Minuteman silos in North Dakota. And the system would be far more powerful than the Patriot missile. Military planners today opt for more precise "hit-to-kill" interceptors, which collide with their targets to knock them out.

Mother Nature favors the aggressor. Three-quarters of an ICBM's half-hour

flight is above the atmosphere. The midcourse phase poses the greatest natural obstacles to efforts to detect and track an enemy missile. The cold temperatures above the atmosphere make it harder for heat-seeking infrared sensors to discriminate among warhead decoys, and booster fragments, whose different masses and densities give them far different temperatures after they reenter the atmosphere. Likewise, it's easier for traditional radar to separate targets from decoys and fragments after atmospheric reentry, where the heat

Scaled-Back Star Wars



MONITORING THE TRAJECTORY

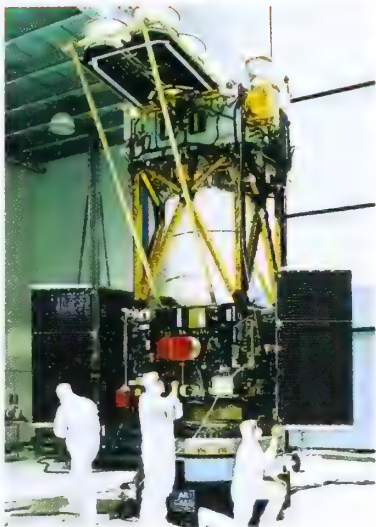
When missiles are detected, information relayed to battle-management stations, computers track the incoming targets. The initial system is designed to track up to 10 incoming missiles.

ier warheads continue to speed toward their target while everything else slows down and tumbles. Advances in radar and infrared technology, however, have gone a long way toward overcoming these hurdles.

One example of an important technological advance is X-band solid-state radar. By operating in the X band

radio spectrum—a
around 10,000
ahertz that's well
e ultrahigh fre-
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employ—the radar
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for the increased distances covered
the speed of the target. ICBMs, with
nge of 3,720 miles and speed of 5
s per second, travel about 10 times
ar as theater missiles and 4 times
er. But the basic radar solution is
same. What's needed is "not a sci-
ic breakthrough but just good old



CRASH COURSE

The Midcourse
Space Experiment
gathers data that
will be needed to
track incoming
missiles above the
Earth's atmosphere

you're looking at,"
says Frank R. Cartier,
manager of TRW
Inc.'s surveillance
programs direc-
torate. "Otherwise,
you're detecting in-
formation off your
noisy detector."

Progress has been made, as well, in
areas beyond detection and track-
ing. Interceptor missiles are small-
er, smarter, and nimbler than
ever before. New thruster
technology makes it easier
to correct course based on
the updated data flow

ground-based system would be barely
above 90%. There would be no guar-
antee that deployment could really
stop Pyongyang from incinerating Los
Angeles or Chicago. Improving the
confidence level to, say, 99.9% would
require more layers of defense and
billions of dollars above the \$39 bil-
lion spent since 1984.

Such a system would violate the
1972 ABM Treaty, however. And some
of the solutions are decades away from
reality. Some Star Warriors would just
upgrade the Navy's sophisticated Aegis
cruisers and station them offshore,
where they could quickly reach missiles
from a Libya or North Korea. But the
Navy might balk until a solid propel-
lant is created. Solid propellants are less
volatile and toxic than liquid propellants.

Another possibility is space-based
lasers. Operating above the atmosphere,
their beams wouldn't be degraded by
air turbulence—a force that could un-
dermine lasers based on planes. But
space-based lasers aren't panaceas.

Like a magnifying glass on a piece of
paper, lasers emit a steady stream of
light to burn through a missile's thin
metal skin. If the target spins, the laser
would have to be enormously powerful
to destroy it.

LEAKY? Gregory H. Canavan, a senior
scientist at Los Alamos National Labo-
ratory, envisions a laser mirror 100
times the size of the Hubble Space Teles-
cope's huge 4-meter mirror. Canavan,
who has been trying to put a laser in

orbit for 25 years, thinks
it's still 20 years off. "The
deployment date of the
darn thing always seems
to recede one year per
year," he sighs.

Will taxpayers wait—
and be willing to shell out
billions more? A \$6 billion
ground-based or sea-based
system might seem a rea-
sonable option to many,
but it won't be perfect.

It's being sold as a shield, but it would
leak, allowing some missiles to get
through. And the CBO estimates that a
more robust layered system with space-
based gadgets could cost as much as
\$60 billion through 2010. Some experts
doubt voters will want to buy such ex-
pensive protection against such a re-
mote threat. "I'm not sure the country
will be willing to commit the resources
needed," says MIT's Postol. If he's right,
despite all the progress made, the drive
for a national security blanket, like the
THAAD test, could run out of gas.

By Stan Crock in Washington



LAUNCHING THE RESPONSE

The battle-management
computers direct the
launch of interceptor
missiles and steer them
toward the targets,
which are destroyed
before they reach U.S.
airspace.

ineering," says Robert M. Stein, a
theon Corp. vice-president who
rsees advanced systems activities.
dvances in infrared sensors—which
ld be located both in low Earth or-
and in higher orbits at fixed points
r the globe—can also help detect
real targets. The long-wave sen-
s now being tested in the Penta-
s Midcourse Space Experiment are
able of picking up tiny heat differ-
es even in the cold environment
ve the atmosphere. The sensors are
led by cryocoolers—tiny refrigera-
s—to 10 degrees Kelvin, or 18F
absolute zero. "You want your
ector to be cooler than the object

from the sensors. But tech-
nology may have progressed
faster than humans can handle it.

Indeed, of the challenges remaining,
helping humans cope with all the new
data is a major one. Pentagon officials
are starting to grapple with the need to
process the overwhelming amount of in-
formation from radars and sensors and to
fuse "pictures" collected at different
wavelengths into one superimage. MIT's
Lincoln Laboratory and Texas Instru-
ments Inc. are looking at possible algo-
rithms to solve the vexing problem.

Even if the system for midcourse-in-
tercept problems were solved, however,
experts say the confidence level in the

The FORD SENIOR PLAYERS Championship's roll call of winners reads like a "Who's Who in Golf History."

It includes Arnold Palmer (1984-85),

Chi Chi Rodriguez (1986), Gary Player (1987), Billy Casper (1988) and Jack Nicklaus (1990). Also on the list is Miller Barber, winner of the 1983 inaugural at Cleveland's Canterbury Golf Club.

Barber ranks second to Lee Trevino in all-time Senior PGA TOUR victories. Miller has 24, Lee 26. But not one of Trevino's has come at the FORD SENIOR PLAYERS Championship, where he is a two-time bridesmaid.

Orville Moody's only PGA TOUR victory was the 1969 U.S. Open. But



Moody owns 11 Senior TOUR titles, including the 1989 FORD SENIOR PLAYERS Championship over the Valley Course at the TPC at Sawgrass in Ponte Vedra Beach, FL.

Former club pro Jim Albus was the surprise winner in 1991. The 1995 Senior PGA TOUR Player of the Year, Jim Colbert, was the 1993 victor.

"The FORD SENIOR PLAYERS Championship and the TPC of Michigan represent two of the finest elements the TOUR and the Senior PGA TOUR have to offer: top-level golf competition at a world-class facility," said PGA TOUR Commissioner Timothy W. Finchem.

"The FORD SENIOR PLAYERS Championship offers the strongest field of the season. Ford sponsorship enables the tournament to contribute significant funding to Detroit-area charities.

"Everything combined makes this a special week on the Senior TOUR," Finchem added.

Last year, Sam Snead's 55-year-old nephew, J.C. Snead, captured the FORD SENIOR PLAYERS Championship. In the process, Snead gained a measure of revenge over the TPC of Michigan, the tournament venue since 1991.

In 1992, Snead led after each of the first three rounds of the



SENIOR PLAYERS CHAMPIONSHIP

Senior TOUR event, setting a course and 36-hole tournament record along the way. He entered the final round with a commanding five-stroke edge over

Bob Charles and Dave Stockton.

Snead still was two strokes in front as he teed off on the 72nd hole, the 417-yard, par-4 18th at the TPC. But he pulled his tee shot into the wetlands guarding the left side of the fairway, leading to a double-bogey six. Stockton's birdie produced a three-shot swing and one-stroke victory over Snead and Trevino, also the runner-up in 1990.

Stockton won again in 1994, joining Palmer as the event's only two-time winners. Palmer's consecutive victories had come at Canterbury, the host course for the first four years.

Snead denied Nicklaus' bid for a second FORD SENIOR PLAYERS Championship last July. Snead once again was the 54-hole leader, holding a one-stroke advantage over Stockton and two-shot edge on Raymond Floyd, Kermit Zarley and Nicklaus.

In 12 previous FORD SENIOR PLAYERS Championships, there had been no playoffs. Snead closed with a 69 as Nicklaus posted a 67, forcing the first.

This time, it was Snead who prevailed. He sank a four-foot birdie putt on the first extra hole to claim his first senior major and the third title of his Senior TOUR career.

The FORD SENIOR PLAYERS Championship is the fourth and final of the year's senior majors, following The Tradition, PGA Seniors' Championship and the U.S. Senior Open. The FORD SENIOR PLAYERS will be contested July 11-14 at the TPC of Michigan.

Located in the Detroit suburb of Dearborn and designed by Nicklaus, the 6,876-yard, par-72 TPC of

FORD SENIOR PLAYERS

Championship

Television Schedule

Thursday, July 11

First Round of Competition

ESPN, 4:00-6:00 p.m.

Eastern Time

Friday, July 12

Second Round of Competition

ESPN, 3:00-5:00 p.m.

Eastern Time

Saturday, July 13

Third Round of Competition

ABC, 2:30-4:30 p.m.

Eastern Time

Sunday, July 14

Final Round of Competition

ABC, 4:00-6:00 p.m.

Eastern Time

Michigan has been home of the FORD SENIOR PLAYERS Championship since 1991.

The year before, Nicklaus established the tournament record at Dearborn Country Club. His winning 261, which featured back-to-back 64s, was 27 strokes under par. Nicklaus' total was the lowest 72-hole aggregate in Senior TOUR history.

Ford Motor Company, whose world headquarters building is just north of the TPC, became title sponsor of the FORD SENIOR PLAYERS Championship in 1993. In May 1995, Ford Motor Company announced it would remain title sponsor of the event through 1998.

The Tournament Players Club is part of the Ford Motor Land Development Corporation's Fairlane Complex. The land on which the TPC now sits was purchased in 1915 by Henry Ford, whose hometown was Dearborn. "The FORD SENIOR



Jack Nicklaus





LAYERS Championship has become a key part of the Ford landscape in Dearborn," said Tom Wagner, Vice President, Ford Customer Communication and Satisfaction. "The tournament is played in the shadow of our world headquarters, which makes it ideal for Ford Motor Company's involvement.

"Ford has a long tradition of supporting charities in the communities where it does business," Wagner continued. "It was a perfectly logical step for Ford to become involved in sponsoring the FORD SENIOR PLAYERS Championship.

"The event site at the TPC of Michigan is on land originally purchased by our founder, Henry Ford. The tournament provides Ford Motor Company with a great opportunity to be a driving force of an event that raises so much money for charities in southeastern Michigan," Wagner concluded.

For the past three years, or since Ford Motor Company became the title sponsor in 1993, the FORD SENIOR PLAYERS Championship has ranked in the top three for money raised for charity among

Senior TOUR events. The 1995 tournament netted \$700,000 for southeastern Michigan non-profits.

"With support from the tournament's Ambassador's Club, amateur player participation in the Pro-Am and the enthusiastic gallery that attends the week-long activities, we hope to continue in 1996 and beyond as one of the top fund-raising events on the Senior TOUR," said tournament chairman

Peter Pestillo, Ford's Executive Vice President, Corporate Relations.

Located just 15 minutes from downtown Detroit, the TPC of Michigan recently became only the second facility to receive the John James Audubon Environmental Steward Award for its efforts to restore a previously degraded area into a nationally significant model of ecological restoration.

Past Winners of the FORD SENIOR PLAYERS Championship

Year	Winner	Course
1983	Miller Barber	Canterbury GC, Cleveland, OH
1984	Arnold Palmer	Canterbury GC, Cleveland, OH
1985	Arnold Palmer	Canterbury GC, Cleveland, OH
1986	Chi Chi Rodriguez	Canterbury GC, Cleveland, OH
1987	Gary Player	Sawgrass CC, Ponte Vedra Beach, FL
1988	Billy Casper	TPC at Sawgrass (Valley Course), Ponte Vedra Beach, FL
1989	Orville Moody	TPC at Sawgrass (Valley Course), Ponte Vedra Beach, FL
1990	Jack Nicklaus	Dearborn CC, Dearborn, MI
1991	Jim Albus	TPC of Michigan, Dearborn, MI
1992	Dave Stockton	TPC of Michigan, Dearborn, MI
1993	Jim Colbert	TPC of Michigan, Dearborn, MI
1994	Dave Stockton	TPC of Michigan, Dearborn, MI
1995	J.C. Snead	TPC of Michigan, Dearborn, MI

EDITED BY JIM ELIS

GETTING THE NET TO HELP BUILD YOUR PORTFOLIO

Sure, there's some truth to those news accounts about penny-stock peddlers and get-rich-quick hucksters lurking on the Internet. The Net has given rise to a new breed of cybertouts trying to hype thinly traded stocks into the ozone, and chat rooms and bulletin boards are teeming with pitches for sand-to-gold schemes.

But if that's the only thing barring you from seeking financial information on the Net, fear not. Cyberspace is vast enough to provide plenty of places to get solid data without encountering the "hot tip" crowd. The World Wide Web, the Net's multimedia section, can provide you with convenient—and often free—access to many major financial publications and other services, such as Morningstar's mutual-fund data. And the low-cost structure of doing business over the Internet has changed the nature of some financial services—enabling discount brokers, for instance, to handle stock trades for as little as \$12, and quote-services to offer real-time data for \$30 a month. That's far less than you would pay elsewhere. So whether you're a Net novice looking for a road map or an experienced surfer looking to get the most out of the Web, there's plenty of reason to handle your finances online.

News is the fuel

that drives the markets, and it's in plentiful supply on the Web. All of the major business periodicals now operate their own Web sites, including *The Wall Street Journal*, *Investor's Business Daily*, *Fortune*, and yes, *BUSINESS WEEK*. But if you want tomorrow's news right now, among these major publications, only the

Journal provides running updates of breaking stories throughout the day. The *Journal's* Interactive Edition not only posts most of the contents of that morning's paper but also allows users to create filters that catch news on specific stocks and to track their investment portfolios. Through July 31, the Inter-

INVESTING



active Edition is free; after that, it will cost \$49 a year (or \$29 for print subscribers).

If you like to check in the markets during the day, there are two sources worth a look. Charter Media's Briefing service (<http://www.briefing.com>) provides updates on stock news and analysis on stock, bond, and foreign exchange markets and the economy. While Briefing's political commentators have a conservative bent, its Story Stock page provides nice analysis of stocks making news. At The Motley Fool, an irrelevant America Online forum that has a fanatical following, also has a free Web site that now includes Lunchtime News report posted around 1 p.m. daily. The

Fool's Web page includes nightly market reports, press synopses of corporate conference calls, but alas, it lacks the popular message board discussions found on AOL.

LONG WAIT. One of the more novel features of the free service is PointCast News, which gathers relevant news from wire services based on a profile of your personal interests. Then "broadcast" your customized news report as a screen saver. You can download PointCast's proprietary software for free from its Web site. Warning: Since news updates can take up to a half hour to download with a 28,800-baud modem, PointCast works best if your company has a fast network connection to the Net or if you pay a flat monthly fee for dial-up access.

If you're too busy to seek out the news, several ve-

will bring it to you E-mail. The best is e.com, which for \$10 to a month will send you flashes on as many as companies of your choosing and notify you when one of your stocks trades above a specified value, much more. For \$180 a year, SEC-Live (<http://www.seclive.com>) will send E-mail alerts whenever one of 15 specified companies' mutual funds makes a filing with the Securities & Exchange Commission. If you can do without the SEC, you can peruse these filings for free on the Edgar site. As of May 1996, every U.S. public company is required to file quarterly earnings and other reports electronically.

Even the nature of the market should come as no surprise that some of the best resources are devoted to high-tech investments. Investor (<http://techweb.com/investor/>), a Web site produced by the CMP Group of trade journals, provides breaking tech news, its 250-stock index, plus information from hot newsletters and its own stable of columnists. And if you want to participate in hip tech discussions, the Silicon Investor boasts lively bulletin-board give-and-take, with links that let you create custom charts of favorite stocks. For its stock tips you're looking for, INVESTtools (<http://www.investtools.com>) provides access to more than 100 of the more reputable newsletters, which you can subscribe à la carte, plus access to bulletin boards. Should your taste run more to mutual funds than stocks, most of the major fund families

Sites for Web-Savvy Investors

SITE/ADDRESS	STRENGTHS
DBC REAL-TIME QUOTES http://www.dbc.com	For \$30 a month, virtually unlimited real-time quotes.
e*BROKER http://www.ebroker.com	Cheapest trades on the Internet: \$12 for any size order.
INVEST-O-RAMA! http://www.investorama.com/	Provides links with about 2,000 investment-related Web sites.
NETWORTH http://www.networth.galt.com	Screen through database of 5,000 mutual funds by 20 criteria.
POINTCAST NETWORK http://www.pointcast.com	"Broadcasts" customized news reports on your PC as a screen saver.
QUOTE.COM http://www.quote.com	E-mail alerts of news and price moves for up to 200 stocks.
SEC'S EDGAR FILINGS http://www.sec.gov	Download 10-Ks, 10-Qs, and other corporate filings to the SEC.
SILICON INVESTOR http://www.techstocks.com	Bulletin boards provide knowledgeable discussion of tech stocks.
THE MOTLEY FOOL http://fool.web.aol.com //fool_mn.htm	Popular site with irreverent market reports and commentary.
WALL STREET JOURNAL http://www.wsj.com	Full text of the newspaper plus breaking news; search 14-day archive.
XENON'S UNIVERSAL CURRENCY CONVERTER http://www.xe.net/currency/	Tells how far your dollars will go against 50 currencies.

DATA BUSINESS WEEK

have erected their own Web sites—though many are little more than marketing gimmicks. One useful site is NETworth, where you can download the prospectus for any of hundreds of funds, access Morningstar performance reports, and screen NETworth's 5,000-fund database for those that meet your criteria.

So how's your portfolio doing today? Free quote services are pervasive on the Net, provided you don't mind

a 15- or 20-minute delay. If you want real-time quotes, the Internet's lower communications costs are enabling providers to pass on the savings: For \$30 a month, DBC Online will give you up to 2,500 real-time quotes per day, plus delayed quotes on futures, options, Canadian, and other foreign issues.

Even after perusing all of these sites, chances are you'll need a few tools to enable you to perform some critical calculations. Toronto's Xenon Laboratories has developed a currency converter that lets you determine how far your dollars will go in marks, yen, or 47 other currencies. Need help valuing options, warrants, and convertibles? Try NumaWeb's Webu-

lator (<http://www.numa.com/derivs/drivex.htm>), which even offers a primer that explains the difference between puts and calls. And the Stock Room (http://loft-gw.zone.org/jason/stock_room.html) assembles such data as domestic- and foreign-market indexes, stock quotes, bond yields, interest rates, and currency tables—and then transforms them into easy-to-interpret graphs.

SAVINGS. After spending all this time surfing the Net, it seems a waste to just place a phone order with your broker (and pay a steep commission for a stock you found via the Net). You don't have to. More than two dozen discount brokers, including Charles Schwab, now allow you to place orders via the Internet. Schwab recently launched its e*schwab service, which charges \$39 to trade up to 1,000 shares. But the cheapest execution by far comes from the new eBroker service: \$12 per trade for any size order. And eBroker is no fly-by-night outfit. It's part of an established Omaha brokerage complex that also operates Accutrade, K. Aufhauser, and Ceres Securities.

There's one catch to these rock-bottom rates: For their lowest prices, eBroker and e*schwab only let you communicate with their customer reps via E-mail. For \$18 per trade, eBroker's sister firm, Ceres, allows you to place orders by either Internet or phone.

One of the best ways to discover other nifty sites is simply to explore. Most of the popular search engines, such as Yahoo! or Magellan, provide links to many investment-related Web sites; Yahoo! alone offers nearly 600 such links. And a few Web aficionados have assembled links of their own: Invest-O-Rama!, the personal Web site of Doug Gerlach, now boasts links to more than 2,000 investment-related sites across the Web. That ought to keep you busy. Happy hunting. *Dean Foust*

SURF 'N BUY Over two dozen discount brokers now allow you to place online orders

TENNIS: SHOULD YOU BUY A LONG RACKET?

So Michael Chang, who popularized the extra-long tennis racket and is the only top-ranked touring pro to use one, was knocked out in the first round at Wimbledon. Does that mean you shouldn't fork over \$200 for an "extended-length," "stretch," "Long-Body," or "superlong" piece of equipment that resembles a rug beater? Hardly. Even if you're only a serious weekend player who's looking for an edge, these new rackets are worth a try.

Power—especially on the serve—is what they're all about. Up to five inches longer from top to bottom than the standard 27-in. racket, the new issues get their extra oomph from faster head speed. Extended rackets now account for 25% of units sold in U.S. specialty stores and pro shops, but because of their higher price—up to double the price of a plain-vanilla racket—they account for 34% of dollar sales, says Bill Lawliss, president of market researcher Sports Research.

The longer rackets, launched nationally last year, have taken off faster than the tennis world's last two major innovations: the oversize racket of the '70s and the widebody of the '80s. Although Dunlop Slazenger was first with the longer models, the match quickly boiled down to Prince vs. Wilson. Together, the pair sold 98% of the extended rackets bought during the first quarter of 1996, according to Lawliss.

Chang's Prince Graphite LongBody, 28 in. long with a 107-sq.-in. hitting area, is the

top-selling extended racket in the world, thanks to hot Asian demand. It's No. 3 in the U.S., behind the Wilson 2.8si Sledge Hammer Stretch (28.5 in. long and 116 sq. in. hitting area) and the Prince Extender Mach 1000 (29 in. long and a huge 124-sq.-in. hitting area). But more-advanced converts prefer a smaller hitting surface, for better control.

In this game, longer has

plains Charlie Peifer, CEO of Prince. "Space Age materials, especially graphite, have made this possible."

Increased power on the serve is estimated at about 10% per extra inch of length by John Powless, a 63-year-old who is top-ranked nationally in the 55-and-over category. Intimidating enough at 6 feet, 5 inches, Powless uses a 29-in. frame that he says also widens the window into his opponent's service box by about 6% per additional inch because the ball is struck at a higher angle. Chang's statistics confirm this. He served 256 aces in the year before he switched

sold unstrung and then turned to give weaker hitters more power. Marge Schinnerer, mother of four who lives Chevy Chase, Md., says Wilson 2.8si Stretch "gives me more power and strength. When you're middle-aged and short, and an average player—like me—it can be a real shot in the arm."

Indeed, the head pro

SPORTS

LaJolla Beach Tennis Club, says Bond, estimates that "50% of the older folks are using longer frames." Explains Prince's Peifer: "All of a sudden, you're 10 years young. Just ask E. Sidney Willis, chairman of the Greenwich (Conn.) Chamber of Commerce, who bought a long racket in late June: 'It puts a little spunk in my serve.'"

TEST DRIVE. Still, longer units take some getting used to. "There's an instantaneous improvement in everybody's serve," says Steve Bromley, head pro at Chicago's Saddle Creek Cycle Club. "But you have to adjust your contact point a little farther forward on ground strokes and volleys."

That's why pros suggest trying out several models before plunking down the big bucks. One, tennis great Bill Jean King, advises players

to emulate golfers: "They miss a few putts and throw away the club. Hit a few serves with a long racket and see if you like it."

Chang does. A few days before he bombed at Wimbledon, the 5-ft.-9-in. pro switched to his longer racket "gives me more reach and snap, power and accuracy, almost as if I'm gaining a little bit of height."

But not too much. In July the International Tennis Federation slashed the 32-inch maximum allowed to 29 inches effective next Jan. 1 for professionals and three years later for amateurs who are playing in sanctioned tournaments. *Keith Feller*



Seniors love extra-length rackets: "All of a sudden, you're 10 years younger"

come to mean lighter. On average, manufacturers have taken two to three ounces off the racket's weight. The Wilson 2.8 and the Mach 1000 weigh only 9.4 oz. and 8.8 oz., respectively, and the Prince Chang is 10.3 oz. "Lighter weight gives you superior leverage and increased head speed for more power," ex-

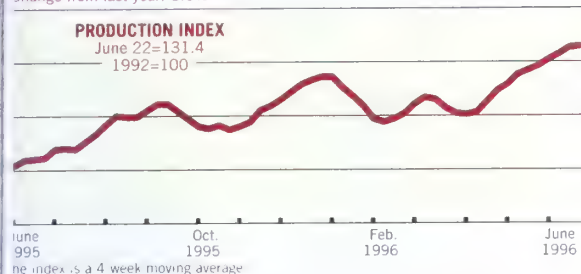
plains Charlie Peifer, CEO of Prince. "Space Age materials, especially graphite, have made this possible."

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Business Week Index

PRODUCTION INDEX

Change from last week: 0.1%
Change from last year: 8.5%



production index edged up slightly during the week ended June 22. However, before calculation of the four-week moving average, the index slipped by 0.7% to 130.7, from 131.6. In the latest week, a decline in the seasonally adjusted output of coal also brought down rail freight traffic. Truck, oil, crude-oil refining, and paper production declined as well.

leading index will be unavailable for an indefinite period.

Source: Bureau of Economic Analysis, Washington, D.C.

ADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (6/28) S&P 500	670.63	666.84	23.3
CORPORATE BOND YIELD, Aaa (6/28)	7.83%	7.90%	5.4
INDUSTRIAL MATERIALS PRICES (6/28)	105.8	106.0	-8.2
BUSINESS FAILURES (6/21)	NA	NA	NA
REAL ESTATE LOANS (6/19) billions	\$508.7	\$507.8	4.9
KEY SUPPLY, M2 (6/17) billions	NA	NA	NA
FEDERAL CLAIMS, UNEMPLOYMENT (6/15) thous	357	360r	-13.1

Sources: Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (7/1)	7.80%	5.15%	6.21%
COMMERCIAL PAPER (7/1) 3-month	5.50	5.50	5.86
CERTIFICATES OF DEPOSIT (7/1) 3-month	5.45	5.48	5.85
FIXED RATE MORTGAGE (6/28) 30-year	8.49	8.50	7.80
ADJUSTABLE MORTGAGE (6/28) one-year	6.11	6.08	5.83
LIBOR (7/1)	8.25	8.25	9.00

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

All data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

RETAILMENT CREDIT

Friday, July 8, 3 p.m. EDT ▶ Consumers probably took on an additional \$8.7 billion new credit in May. That's the median cast of economists surveyed by MMS International, one of The McGraw-Hill Companies. The strong gain is suggested by the ease in retail sales, especially for durable goods, which are typically bought on credit. Debt increased by a relatively small \$6.6 billion in April, but the slower growing pace may have been an offset to record tax payments made by individuals in April. Some consumers are starting to be squeezed by too much debt: First-quarter delinquency rates on credit cards jumped to the highest level in 15 years.

UNEMPLOYMENT CLAIMS

Thursday, July 11, 8:30 a.m. EDT ▶ New claims for state unemployment benefits probably stood at a 325,000 pace for the week ending July 6. That's below the 350,000 average for filings over the past few weeks, but the latest survey period will include Independence Day, when state offices are closed.

RETAIL SALES

Friday, July 12, 8:30 a.m. EDT ▶ The MMS median forecast projects that retail sales increased by just 0.2% in June, following a strong 0.8% advance in May. The slower pace is indicated by the weekly survey of retailers and steady sales of motor vehicles.

Excluding cars, store receipts likely increased by 0.3% in June, the same gain posted in May.

PRODUCER PRICE INDEX

Friday, July 12, 8:30 a.m. EDT ▶ Producer prices of finished goods were probably unchanged in June, after falling 0.1% in May. Lower energy prices will likely lead the decline. Excluding food and energy costs, core producer prices likely edged up 0.1% in June, after no change in May. Further back in the production cycle, prices for intermediate supplies and raw materials probably declined in June because of the collapse in copper prices following the scandal at Sumitomo Corp.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (6/29) thous. of net tons	1,986	1,983#	6
AUTOS (6/29) units	133,237	143,127#	7.2
TRUCKS (6/29) units	111,338	118,800#	7.8
ELECTRIC POWER (6/29) millions of kilowatt-hrs	NA	70,688#	NA
CRUDE-OIL REFINING (6/29) thous. of bbl/day	NA	14,252#	NA
COAL (6/22) thous. of net tons	18,470#	20,189	7.5
PAPERBOARD (6/22) thous. of tons	884.0#	874.4	-8.3
PAPER (6/22) thous. of tons	819.0#	820.0r	-1.8
LUMBER (6/22) millions of ft.	471.9#	480.8	11.4
RAIL FREIGHT (6/22) billions of ton-miles	24.6#	25.5	-0.4

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA1, SFFPA2, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (7/2) \$/troy oz.	381.950	383.800	0.9
STEEL SCRAP (7/1) #1 heavy, \$/ton	138.50	138.50	1.4
COPPER (6/29) ¢/lb.	99.3	105.1	-30.3
ALUMINUM (6/29) ¢/lb.	70.0	69.8	17.2
COTTON (6/29) strict low middling 1-1/16 in., ¢/lb.	77.64	79.88	-12.1
OIL (7/1) \$/bbl	21.30	19.88	22.4

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (7/2)	110.13	109.55	85.99
GERMAN MARK (7/2)	1.53	1.53	1.39
BRITISH POUND (7/2)	1.56	1.54	1.60
FRENCH FRANC (7/2)	5.16	5.17	4.84
ITALIAN LIRA (7/2)	1535.5	1534.9	1618.3
CANADIAN DOLLAR (7/2)	1.36	1.36	1.37
MEXICAN PESO (7/2)	7.583	7.603	6.220

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

HOT TRANSCRIPTS

Missed the chance to talk with Oracle founder and CEO **Larry Ellison** in a Business Week Online live conference? Or maybe you were away when BW economist **Bill Wolman** gave his latest investment advice.

It's not too late to find out what they—and other important newsmakers—had to say about today's top issues. Just log on to BW Online on America Online and download the transcript of any of our past conferences—more than 160 to choose from.

Here's a sampling of what you'll find—and we're adding more every week:

Dilbert

Scott Adams, creator of the wildly popular comic strip lampooning management, shoots from the hip—5/29/96

Hot Growth Stocks

Insights on investing in small companies from Gary Pilgrim of PBHG Growth Fund—5/19/96

Online vs. the Net

Will the Web make online services obsolete?—4/10/96

Showroom Revolution

How auto malls—and the Net—are changing the way you shop for cars, with J.D. Power's Donald Keithley—2/11/96

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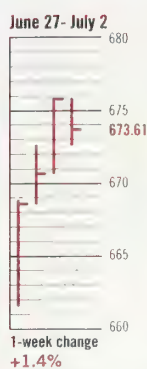
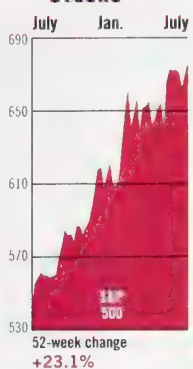
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Investment Figures of the Week

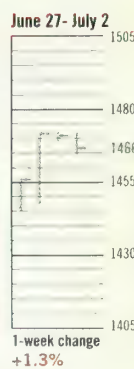
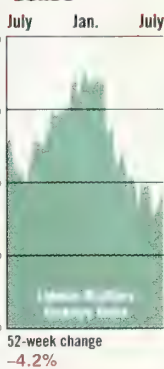
MARKET COMMENTARY

Stocks enjoyed a major surge July 1, with the Dow Jones Industrial average posting its largest gain since mid-March. The index climbed 75 points as traders cheered by improved factory output—and expectations of higher profits. However, stocks fell back on July 2 because of a rise in high-tech stocks, partly Digital Equipment. Yields on 10-year bonds fell below 7% on July 1, though improved economic growth drove yields up again in the session that followed.

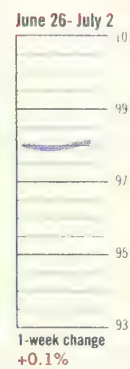
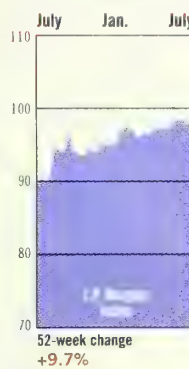
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS

	Latest	% change Week	% change 52-week
INDUSTRIALS	5720.4	0.7	23.9
SMALL CAP COMPANIES (S&P MidCap Index)	237.0	2.5	19.3
MID-CAP COMPANIES (Russell 2000)	346.9	2.1	21.8
LARGE CAP COMPANIES (Russell 3000)	384.2	1.7	23.2

INTERNATIONAL STOCKS

	Latest	% change (local currency) Week	% change (local currency) 52-week
FINANCIAL TIMES 100	3725.7	0.8	9.7
NIKKEI INDEX	22,348.0	-1.4	50.7
TSE COMPOSITE	5061.5	0.7	11.2

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.30%	5.22%	5.67%
30-YEAR TREASURY BOND YIELD	6.93%	7.04%	6.60%
S&P 500 DIVIDEND YIELD	2.13%	2.15%	2.44%
S&P 500 PRICE/EARNINGS RATIO	19.4	19.1	16.9

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day moving average	629.1	627.3	Positive
Stocks above 200-day moving average	62.0%	58.0%	Neutral
Speculative sentiment: Put/call ratio	0.60	0.67	Neutral
Insider sentiment: Vickers sell/buy ratio	2.52	2.49	Negative

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

MONTH LEADERS

	% change 1-month	% change 12-month
BEVERAGE DRINKS	7.3	55.3
EXPLORATION AND PRODUCTION	7.0	16.6
PROPERTY-CASUALTY INSURERS	5.9	26.1
PERSONAL LOANS	5.6	45.2
TABACCO	5.5	36.7

Strongest stock in group

	% change 1-month	% change 12-month	Price
COCA-COLA	7.3	54.9	49 ³ / ₈
BURLINGTON RESOURCES	12.5	15.9	42 ³ / ₄
ALLSTATE	10.1	57.0	46 ¹ / ₂
HOUSEHOLD INTERNATIONAL	9.4	53.0	75 ³ / ₄
PHILIP MORRIS	5.5	41.0	104 ⁷ / ₈

MONTH LAGGARDS

	% change 1-month	% change 12-month
STEEL MINING	-15.1	7.0
PACKAGING	-8.3	-14.8
POLLUTION CONTROL	-6.6	2.2
WIRELESS	-6.5	-14.7
ALUMINUM	-6.0	7.6

Weakest stock in group

	% change 1-month	% change 12-month	Price
ECHO BAY MINES	-20.4	19.4	10 ³ / ₄
CALIBER SYSTEM	-11.1	-18.2	33
WMX TECHNOLOGIES	-7.8	14.5	32 ¹ / ₂
INLAND STEEL INDUSTRIES	-9.8	-36.1	19 ¹ / ₂
ALCAN ALUMINUM	-7.3	0.0	30 ³ / ₈

MORNINGSTAR INC.

MUTUAL FUNDS

LEADERS

	% 4-week total return
WINTHROP EASTERN EUROPEAN EQUITY	7.8
WINTHROP PINCUS JAPAN OTC COMM.	5.4
WINTHROP SELECT NATURAL GAS	5.3

LAGGARDS

	% 4-week total return
INVESCO STRATEGIC GOLD	-18.2
UNITED SERVICES GOLD SHARES	-17.0
RYDEX PRECIOUS METALS	-16.7

	% 52-week total return
WINTHROP SMALL CAP EQUITY	75.0
WINTHROP SELECT EQUITY	67.8
WINTHROP GLOBAL HEALTH CARE	66.2

	% 52-week total return
STEADMAN TECHNOLOGY GROWTH	-28.0
STEADMAN AMERICAN INDUSTRY	-19.1
STEADMAN INVESTMENT	-14.7



RELATIVE PORTFOLIOS

Percentages represent the percentage change in the value of \$10,000 invested one year ago in each portfolio.

Percentages indicate daily total returns.

U.S. stocks
\$12,642
+1.05%

Foreign stocks
\$11,655
+0.29%

Money market fund
\$10,533
+0.11%

Treasury bonds
\$10,231
+2.39%

Gold
\$10,188
-0.74%

Data on this page are as of market close Tuesday, July 2, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of

market close July 1. Mutual fund returns are as of June 28. Relative portfolios are valued as of July 1. A more detailed explanation of this page is available on request. r=revised

MICROSOFT: A LESSON IN MANAGEMENT

Passion and pragmatism are an unusual combination of traits in a CEO. But the ability to run hard and then reverse course is allowing Microsoft's Bill Gates to make the jump from PCs to the Internet. It is a leap worth studying, for few leaders in business or in government are able to make such a cosmic adjustment either conceptually or in practice. We tend to fight the last war, repeat the same behaviors, and solve the same problems. It can be deadly.

Gates came close to blowing it (page 56). Dominant in personal computer software, Microsoft Corp. spent the early years of Net growth obsessing over Windows and cooking up proprietary ways of doing things in cyberspace. While technopsters were on the World Wide Web, Gates was finishing Windows '95 and beating back government regulators worried about Microsoft's alleged anticompetitive practices. Based in Redmond, Wash., Microsoft was far from Silicon Valley, where the Net was hot. And, although only 37 in 1993, Gates was a generation away from Gen-Xers using the Net. By the early '90s, Netscape Communications, Sun Microsystems, Yahoo!, and a host of startups had already taken control of the Net.

Think IBM. General Motors. Philips. Apple Computer. Olivetti. Corporations with market dominance that lose it when technology and the markets change everything before them. That was Microsoft at this point—an amazing 20-year success, dominant in its field, stupendously profitable. And nearly blindsided. By the time Win95 was shipped in August, 1995, Netscape had gone public, launching a bull market in Internet stocks. Netscape's Web browser had Microsoft-like dominance, and Sun's Java software was becoming the Net standard.

Gates grew up watching IBM falter and Digital Equipment nearly crash and burn—up close and personal. He knew it

could happen to Microsoft and created a corporate culture that spent little time celebrating a project's completion. Instead of beer busts, Microsoft launched postmortems over what should have been and what could be next time. This process helped save the company. In 1994, at an executive retreat, young employees boldly spoke out about Microsoft's failure to deal with the Net—and implicitly, Gates's failure to lead them into this new territory.

Gates did a 180. He replaced his passion for product with pragmatism for business. Entrepreneurs usually are willing for obsession and are often wedded to a position. Think John Manzi and Lotus Notes, Ken Olsen of DEC, or Steve Jobs at the Macintosh. As new Web software standards threatened to make Windows irrelevant, Gates agreed that the Internet was going to drive demand for PCs and software. He opted to play by the Internet's rules, not the PC rules Microsoft had written with Windows. Gates ordered that Microsoft become Web-centric, dumping that which didn't fit, and reshaping everything else. In Silicon Valley parlance, Gates showed he was willing to "eat his young" to stay on top.

Gates may yet fail. Microsoft is working its 20,000 people around the clock to develop browsers, Web servers, and other Net software. Every week brings another Microsoft Internet announcement, from joint venturing with General Electric Co. on MSNBC, to publishing Michael Kinsley's *Slate* cyberzine. Gates is late, and he has to battle Sun's Scott McNealy and Netscape's Jim Clark, both students of Silicon Valley history, too. But at least Gates is in the game now, second. In a world where change is the constant, CEOs and political leaders should take note. Pride often goeth before a fall. Bill Gates was wise enough not to let it happen to Microsoft.

CHINA AND TAIWAN: A WELCOME CALM

That silence you hear across the Taiwan Strait is the sound of Beijing and Taipei making up. After missile tests, naval maneuvers, and threats, the two are easing into a rapprochement. It's a welcome development in Asia and may pave the way for calmer relations between the U.S. and China (page 52).

First came the toning down of rhetoric. Taiwan President Lee Teng-hui, a vocal critic of Beijing during the recent presidential election, is now more cautious in his statements. Voices from within the new cabinet are promoting a strong pro-unification line since the missile tests last spring. Some politicians are calling for investors to "go West"—i.e., invest in the mainland. A number of Taiwan's largest companies, including the giant Formosa Plastics Group, are pressuring Taipei to smooth ties with China and allow them to invest several billions of dollars on the mainland.

To soothe China, Taipei is backing off from its bid to enter the U.N., a move toward independence that enraged

Beijing. Now Taipei talks only of joining international economic organizations such as the World Bank and the International Monetary Fund. Beijing also is toeing a softer line. The threats are gone, and talk is mostly about investment and economics, not war and invasion. There is a move to simplify airline connections between the two, and recently both sides inked a joint oil exploration deal.

Relations between China and the U.S. are also moving to a quieter footing. After months of threatening sanctions and countersanctions, an intellectual-property agreement was just signed. And President Clinton is set to grant most-favored-nation status. Without much fanfare, Beijing has agreed to sign the nuclear test ban treaty. If American politicians can refrain from stirring the pot and attacking China this election year, and Chinese officials show restraint when they take over Hong Kong in 1997, the calm may be extended into the future.

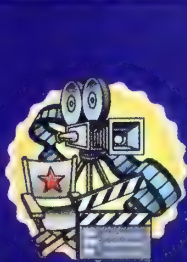
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STOCK OPTIONS

Why they're booming. How to use them.

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- ▶ How they're taxed
- ▶ Do they really buy corporate loyalty?

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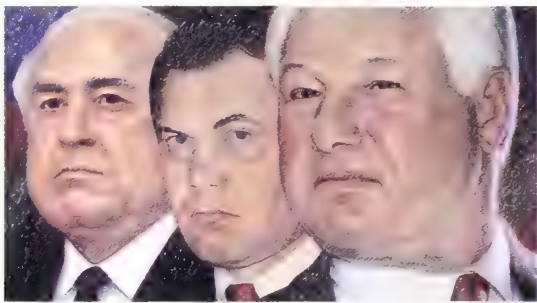
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assigns power to his
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BusinessWeek

JULY 22, 1996

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STOCK OPTIONS
Why they're booming.
How to use them.
When to cash out

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80 OPTIONS FOR EVERYONE

The stock options game has a lot of new players. Many more companies are figuring that giving employees far from the executive suite a crack at stock options will help persuade them to work harder and more productively. It sounds great. But options hold snares as well as blessings and need careful handling by employer and employee alike if they are to benefit both

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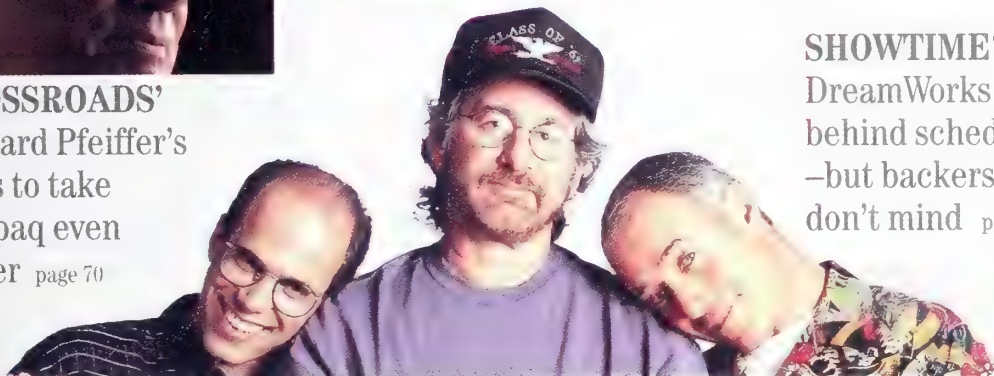


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A HUGE, CLUNKY, REVOLUTIONARY TV

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Up Front

EDITED BY LARRY LIGHT

SLUGFESTS

THE PEACOCK RUFFLES ITS AFFILIATES

SOME NBC AFFILIATES are complaining about the network's plans to air plugs for its new cable venture with Microsoft, MSNBC. They fear the result would be to steer audiences away from member TV stations to all-news MSNBC, which will boast such NBC stars as Tom Brokaw and Jane Pauley.

A number of affiliates want the plugs killed. One,

Boston's WHDH, says it may even yank MSNBC promos. Says Michael Carson, WHDH general manager: "We have a real serious problem with our NBC relationship."

The network isn't saying much about how it will use NBC to promote MSNBC, set to debut July 15. Member stations expect most plugs will



ers to switch to CNBC, its business-news cable channel, for more basketball highlights.

Hoping to calm affiliates, NBC Network President Neil Braun told them in a July 1 letter that after the plugs start running, he'll gauge whether viewers defect to MSNBC as a result.

If so, says the letter obtained by BUSINESS WEEK, NBC will make unspecified adjustments. The dissident affiliates aren't assuaged, however, calling this a stalling tactic. *Andrew Ross Sorkin*

I-WAY PATROL

INSURANCE ALERT: SLIPPERY PITCHES

LIFE INSURANCE SALES FOLK are taking to the Internet to flog their policies. However, state regulators, afraid of end runs by unlicensed sharpies, have put cops on the beat.

The regulators say that they have turned up a number of suspicious pitches, although at this early stage, they haven't filed any charges. In Utah, for instance, regulators are investigating an unnamed information service that claims to be using the Internet to provide premium quotes on behalf of top-drawer insurers—a service which doesn't require a license. The problem is that the company also "takes applications and accepts premiums," says Dixon Larkin, Utah's deputy commissioner of insurance. That requires state licensing. Maryland is investigating two unnamed agents for selling on the Internet without obtaining a license.

Aside from possible fraud, regulators are concerned that consumers buying from an

unlicensed source won't be legally protected. Dozens of insurance companies fail every year. If an insurer is unlicensed, policyholders won't be entitled to a share of the busted company's assets or be repaid from a state's guaranty fund, which is set up for assetless failures.

To better educate consumers, such states as Illinois, Michigan, and Colorado are developing home pages on the Web. These pages will provide specifics on licensing requirements for both agents and insurance companies. *Lisa Sanders*



AMERICA THE GREEN

BURN A WATT, WIN A TOASTER

BOOST THE AIR-CONDITIONER, and you may win a prize from Centerior Energy. Quite a turnabout from the usual utility marketing that rewards customers for saving energy, not using it.

The 930,000 residential customers of Centerior, the utility serving much of northern Ohio, can soon earn frequent-flyer-like points for every kilowatt hour used—redeemable for an electrical appliance. Prizes will tend to be small: An average customer using 500 kilowatt hours monthly can, over 14 months, win only a night light. A heat

pump would take decades.

The company says it's aiming to build customer loyalty as deregulation brings stronger competition. Despite environmentalists' alarms, it denies that people will use more power—they'll simply get energy-efficient prizes for what they use now. Meanwhile, the Public Utilities Commission of Ohio is examining whether the offer, by favoring high-energy users, violates a state law that bans discriminatory pricing—a notion that Centerior Energy contests. *Zachary Schiller*



THE HORROR
An idle out

THE LIST BIG LABOR'S BIG CARROT

Democratic-leaning political action committees, particularly labor unions', are coming on strong lately. Only one corporate PAC, United Parcel Service, is left in the top five. Most of the change came in 1996 as Republicans'

electoral fortunes waned. With health-care reform dead, the American Medical Assn. has dropped off the top-donors' roster. Most of this election cycle's heavy spending will be in 1996's second half. Figures are in millions.

24 MONTHS 1993-1994

UNITED PARCEL SERVICE	\$2.65
AFSCME**	2.52
TEAMSTERS UNION	2.48
AMERICAN MEDICAL ASSN.	2.38
NATIONAL EDUCATION ASSN.	2.26

17 MONTHS 1995-1996*

AFSCME**	\$1.20
UNITED PARCEL SERVICE	1.17
ASSN. OF TRIAL LAWYERS	1.16
TEAMSTERS UNION	1.13
ELECTRICAL WORKERS UNION	1.07

*Through May 31 **American Federation of State, County & Municipal Employees

DATA: FEDERAL ELECTION COMMISSION; BUSINESS WEEK

MORE AND MORE BUSINESSES ARE FINDING GOLD IN TENNESSEE.



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TENNESSEE

HONCHOS

SO MUCH FOR THE OLD BOYS' CLUB

CHIEF EXECUTIVES HARDLY ever trash each other. Except for Al Dunlap, who just did that to AT&T Chairman Robert Allen. It's part of his general barrage against his peers in the Conference Board's magazine, *Across the Board*, in one of the publication's verbatim interviews of business notables.

Dunlap, former head of Scott Paper, knocks other CEOs for failing to defend business against attacks on downsizing. He feels downsizing is necessary for American competitiveness. "I'm personally outraged at the

conduct of CEOs ducking, bobbing, and weaving," says Dunlap.

Then he singles out Allen for seeming to waffle on the number of firings at the phone company. "Every time Robert Allen opens his mouth, he's a danger to himself," Dunlap told the publication. "He's the world's worst spokesman, and he actually puts the cause back. He should lock himself in a closet." Allen declined to comment on Dunlap's outburst. The magazine didn't solicit an AT&T interview for its article.

Dunlap, who has a book coming out, *Mean Business: How I Save Bad Companies and Make Good Companies Great*, is weighing job offers but won't say where. Likely not from AT&T. *Joseph Weber*



DUNLAP TO ALLEN: Shut up

AFTERLIVES

GOING FOR ANOTHER KIND OF GOLD

THE CROWDS, THE celebrities, the pageantry, the media spotlight—all that is up ahead for Atlanta Olympic Games chief Billy Payne. Back in 1984, the center of the Olympics was Peter Ueberroth. Will the head of the Los Angeles games even show up in Atlanta? Only, he says, if his schedule permits.

These days, Ueberroth, 58, who just returned from a London deal-making trip, is consumed with the investment outfit he heads, Contrarian Group. The Newport Beach (Calif.) firm puts money into troubled or little-known companies, buffs up operations, and often takes



UEBERROTH: Deal guy

them public. Consider Ambassadors International, a Spokane (Wash.) tour packager whose stock is up 50% since going public in August. Ueberroth is also a co-chairman of Doubletree, a hotel-management company posting strong profits.

Ueberroth's '84 Summer Games, the first to be all-privately funded, rang up a \$222 million surplus. One reason: He cut the corporate sponsors list to just blue-chippers and hiked their fees. Next came a half-decade as Major League Baseball Commissioner. A notable disappointment was his bid to rebuild South Central Los Angeles after the 1992 riots. *Lisa Sanders*

INFLATION WATCH

HEY, ALAN, IS THIS A STRAW IN THE WIND?

THE FEDERAL RESERVE HAS long been looking for signs of resurgent inflation. Could this be one? A good many more small businesses are raising prices than lowering them lately, says the National Federation of Independent Business' monthly survey—22% boosted prices in June, while 12% reduced them, for a net increase of 11% (seasonally adjusted).

Since small enterprises contribute 40% to gross domestic product, this bears watching, although economists say it's too early to tell if this is a trend. To NFIB chief economist William Dunkelberg, this doesn't pose "a serious inflation threat." But this year until May,

when the net increase hit 15%, it had been in single digits. The survey says a net 16% plan to raise prices in the third quarter.

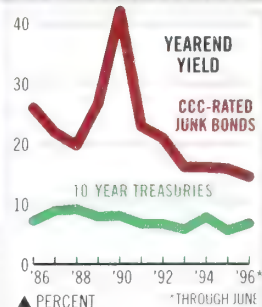
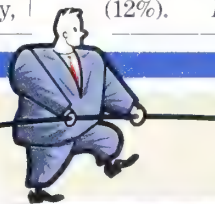
Some of the surge comes from the ever-fluctuating commodity area, particularly in the agriculture sector (36%). Drought has led to higher feed costs. Young's Farm of Dewey, Ariz., plans on raising turkey prices by 10¢ a pound, up from \$1.59 last year. Rain may cure that. But there's acceleration in sectors where hikes may stick, such as retail (18%) and transportation (12%). *Lisa Sanders*



THE BIG PICTURE

RISKY BUSINESS

Junk bonds pay the highest yields to compensate you for the risk that they may default. But thanks to the still-buoyant economy, that risk has diminished somewhat—and so have junk yields, even on CCCs, the most speculative grade.



DATA: BOND INVESTORS' AS IN SALOMON BROTHERS, INC.

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THE WORLD NEEDS NAGGING ON SOME ISSUES

As convener of a congressional hearing on child labor and ecological degradation, I take exception to your assertion that raising such issues is "nagging" ("The U.S. is becoming a global nag," Editorials, July 1). You presume such concerns interfere with the real business of the world, which is business. Where have we heard that before?

I couldn't agree with you more that the Helms-Burton anti-Cuba act is "an election-year sop by politicians to Florida's Cuban voters." But you wrongly include child labor, the environment, and other issues in your attack. Human rights and environmental protection are legitimate U.S. concerns, whether they are handled internationally—as would be most effective—or by the U.S. alone.

Portions of the business community may look solely to the financial bottom line, but policymakers have an obligation to raise additional considerations in the discussion of trade and foreign policy.

George Miller (D-Calif.)
 House of Representatives
 Washington

FALSE FLAG-WAVING AT WAL-MART?

Your article missed the point our union was trying to make about the buying practices and deceptive advertising program of Wal-Mart Stores Inc. ("Unions that live in glass houses..." Up Front, July 1).

Companies that employ United Food & Commercial Workers members do sell merchandise manufactured in foreign countries, but they don't do so by wrapping themselves in the American flag with misleading advertising practices and in-store promotions—as Wal-Mart does. Wal-Mart boasts how it "brings it home to the USA." UFCW would like to add to that slogan: "...from the USA."

Samuel J. Talarico
 President
 District Union Local One
 Utica, N. Y.

CORRECTIONS & CLARIFICATIONS

In an illustration accompanying "A star is reborn" (Entertainment, July 8), locations of Disney's New Amsterdam Theater and the Bertelsmann building were wrong. Here are their correct Times Square locations:



In "Why bailouts are bad medicine" (Economic Viewpoint, July 8), the list of companies where fraud has been discovered was meant to include Sumitomo Corp., not Sumitomo Bank Ltd.; and Daiwa Bank Ltd., not Daiwa Securities Co.

'THE FAA BREACHED THE TRUST OF THE AMERICAN PEOPLE'

We support your call to redefine the central mission of the Federal Aviation Administration ("Help wanted: A new transportation head," Editorials, July 1).

By failing to inform the public about the safety and maintenance problems revealed during ValuJet Airlines Inc.'s three years in operation, the FAA breached the trust of the American people. President Clinton and Congress must instruct the FAA to review its policy on new airlines, in order to ensure maximum supervision throughout the startup process. We firmly believe new airlines should be issued provisional certificates during their first 12 to 24 months of operation, restricting their growth until they can establish an exemplary safety and maintenance record.

The FAA's ongoing mismanagement of

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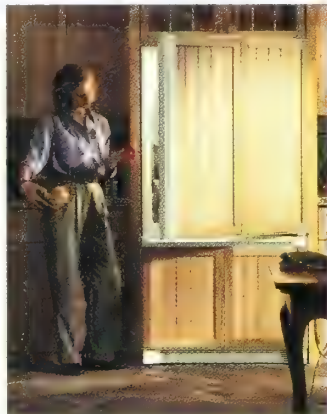
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Readers Report

the ValuJet fiasco makes crystal-clear the need for a significant change in the agency's leadership and direction. After seeing the tragic consequences of inaction, can the American people afford to wait?

Ivan Michael Schaeffer
President and CEO
Woodside Travel Trust
Bethesda, Md.

THE MESSAGE IS THE MEDIUM

Communication has gone from hieroglyphics, smoke-and-mirror signals, totems, and carrier pigeons to print, Morse code, broadcast, computers and all the things you outlined in "The new hucksterism" (Cover Story, July 1). But one thing hasn't changed since the beginning of time: You have to get the message over.

That's why most advertising doesn't work—the failure to communicate to a specific niche market. When people in the ad business start remembering this and stop trying to win awards, they will find they can get a great deal of satisfaction by producing results for the companies paying them.

Edgar S. Spizel
Spizel Marketing/Advertising/
Public Relations
La Jolla, Calif.

GIVE THOSE GRAINS A GRAIN OF THOUGHT

I take issue with the idea that an increase in meat consumption represents an improvement in diet ("The new economics of food," Cover Story, May 20). Diets that were formerly mostly grains, vegetables, and fruits have certainly not been improved by the addition of, or increase in, animal protein. These diet "improvements" have raised the rate of heart disease and cancer in both men and women in countries such as Japan. Hardly an improvement!

In addition, it takes five times as much grain to feed people when the grain is cycled through an animal. Putting that half-pound steak on your plate at a cookout uses enough grain to feed five hungry people for two or three days.

Susan Siemers
South Bend, Ind.

NO TAX DUE—UNTIL YOUR PIGGY BANK IS FULL

I believe Gary Becker is on the right track in proposing that lower-income

households be exempt from federal income taxation ("Yes, pass a flat tax—but clamp a lid on spending," Economic Viewpoint, July 1). What is more important, however, is wealth accumulation. Why not exempt households from taxation until they have accumulated three years' income in a privately managed, government-sponsored Social Security fund that can be drawn on in an emergency? Allowing people to accumulate a personal safety net—and setting up the means by which that can be accomplished—would reduce (perhaps eventually eliminate) the need for government to fill this role.

Edward J. Dodson
Cherry Hill, N.J.

Professor Becker has perhaps forgotten the public spending agenda is also determined by elections premised on majority rule. If an electoral majority votes for more government spending and hence a larger public sector, one must also reason that this majority has both the will and the intellect to provide the necessary fiscal means.

A flatter tax will redistribute income and wealth from the bottom to the top, thereby exacerbating America's widening gap between the rich and poor. Rising inequality has a way of nullifying future expectations about productivity and efficiency, even with a flatter tax.

Romie Tribble Jr.
Professor of Economics
Spelman College
Atlanta

FOR PROSPERITY, THE U.S. NEEDS GROWTH—AND TRAINING

In his column "Is worker training really the answer?" (Economic Viewpoint, June 17), Robert Kuttner concludes that economic growth—not education and training—is the key to improving the economic prospects of the American workforce.

We agree wholeheartedly. Enhanced training is, however, an important stepping stone along the path toward a strong growth economy. Mr. Kuttner, in dismissing training as an economic answer, fails to make the connection between the two.

Enhanced worker training and education won't lead directly to prosperity, but they will allow businesses to take advantage of new technologies, thereby increasing bottom lines, creating new jobs, and raising the living standards of workers. Training also provides employment security and the ability to move smooth-

ly from job to job or from company to company. Smart manufacturers are providing such training not because they are looking to cultivate a civic-minded image, as Mr. Kuttner suggests, but because training is a key ingredient to competing successfully in the 1990s.

Jerry J. Jasinowski
President
National Association
of Manufacturers
Washington

THE BENLATE BROUHAHA: DUPONT'S VIEW

The Commentary by Legal Affairs Editor Mike France presents only one side of the story regarding DuPont Co. and its fungicide, Benlate ("Corporate litigation: Playing hardball is one thing..." News: Analysis & Commentary, July 1).

Mr. France implies that DuPont holds itself "above the law" and says our trial tactics were "inexcusable." He has fallen into the same trap that Judge Robert Elliott did in Georgia—buying the plaintiffs' attorneys' strategy, which focuses not on the facts of the case, but on allegations of "discovery abuse."

These allegations are groundless. Millions of DuPont documents have always been available to plaintiffs' attorneys, not only in the Georgia case but also in dozens of other Benlate litigation cases.

Stacey J. Mobley
Senior Vice-President
External Affairs
DuPont Co.
Wilmington, Del.

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IT'S AMAZING WHAT
WE CAN DO TOGETHER

BROKEN PROMISES

An Unconventional View of What Went Wrong at IBM

By D. Quinn Mills and G. Bruce Friesen

Harvard Business School Press • 210pp • \$22.95

IBM: HISTORY, BUT NO LESSON

The CEO of IBM is frustrated. There's a huge gap between his company's stated goals and its achievements. The stock has tanked, morale is in the basement, and the company's products have not kept up with the changing market. Customers complain that new models are taking too long to emerge. Worse, they're starting to crab about a maddening bureaucracy: Simple questions get routed through 18 different IBMers. To regain technological leadership, the CEO pushes for an overhaul of the product line, but the sales force worries about switching from high-margin products to new technology with lower margins.

Sound familiar? Surely this must be the tale of John Akers, the CEO ousted by IBM's board in 1993, or perhaps the scenario of the first months of his successor, Louis V. Gerstner Jr. Nope. The IBM satchem here is none other than the legendary Thomas J. Watson Jr. And the time is the early 1960s—just before the most profitable period in IBM history. So begins *Broken Promises: An Unconventional View of What Went Wrong at IBM*, in which Harvard business school professor D. Quinn Mills and Andersen Consulting executive G. Bruce Friesen probe the roots of Big Blue's woes to provide lessons for other big corporations. Unfortunately, after a good start it quickly turns into an academic and too often dry account that provides much less than it promises.

What went wrong, argue the authors, was that IBM went back on two unwritten commitments it had made over the years to customers and employees. Mills and Friesen call these "singleness" and "loyalty." IBM convinced customers that only Big Blue could handle all their computing needs—from printer ribbons to mammoth computers that required special air-conditioned rooms. It guaranteed top-notch products and blanket

service by scores of IBM engineers—all working at the customer's office. The customer rented the equipment, and IBM took care of everything.

For employees, IBM's job security was legendary. It wasn't unusual to find two generations of the same family represented. There were never any layoffs or unions. And this loyalty to employees buttressed the promise to customers: A happy and motivated workforce meant good service.

The common wisdom that IBM stumbled because it fell behind in technology is wrong, say Mills and Friesen. Yes, IBM relied too long on mainframes at a time when rapidly advancing semiconductor technology—some of it invented at IBM—was quickly changing the computer industry. But Big Blue's failure to respond, they suggest, was a symptom of a more fundamental problem: IBM's shift from rental to sales in the early 1980s began a dramatic change in the nature of the customer relationship, making the giant just another computer maker competing on price.

The bond between the company and its workers began to fray with massive reorganizations in the 1980s, followed by layoffs. An unanticipated consequence was to sever long-term relationships employees had with customers—a link that might have kept IBM better tuned into market changes, say the authors.

A consultant at IBM through much of the 1970s and 1980s, Mills clearly knows the pre-Gerstner era. He and Friesen, his research assistant when he was at Harvard, interviewed numerous executives and had access to internal documents. When looking at IBM from a historical perspective, the authors excel.

For example, they make a persuasive case that the seeds of IBM's disastrous performance in the early 1990s were planted in the rapid expansion and shift to outright computer sales begun in the early '80s.

Readers expecting the inside scoop on one of the great business disasters of the 1990s, though, will be disappointed. The book is academic to its core and devoid of any IBM personalities. Moreover, the authors rarely quote IBMers whom they've interviewed. In the preface, they thank Akers for his contribution, but there's not a quote from him in the book. Indeed, Akers, the man often held most culpable for IBM's woes, gets off with barely a scratch.

The most glaring flaw is the book's claim to having an unconventional view of IBM. Rather, the authors oversimplify the widely held understanding of why IBM cratered in the early '90s. True, most observers focused on the decline of the mainframe and IBM's technological ineptness. But IBM's hubris has also been widely reported, as has the broken tradition of job security.

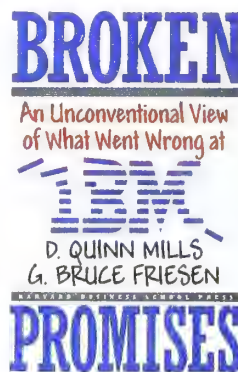
What's more, the authors give remarkably short shrift to present-day IBM, discussing Gerstner and his actions only in the penultimate chapter. There they provide no more than a superficial examination of issues. At times, Mills and Friesen just don't seem to know the high-profile company. They

misspell the name of the executive who led the development of the IBM PC, Don Estridge. Later, they say that small-to-medium-size companies feel ignored by IBM and question whether the company is going to miss out on these hot-growth outfits in the future. In fact, Gerstner & Co. have made sales to this segment one of IBM's top priorities.

The lessons of IBM's experience are now common wisdom among executives—listen to customers, understand your business, fight bureaucracy, etc.—and, sad to say, the authors add little to these. Indeed, the key broken promises here are those of the authors of this rather conventional account of IBM.

BY IRA SAGER

Sager covers computing for BUSINESS WEEK.



THE AUTHORS OVERSIMPLIFY THE COMPANY'S PAST AND NEGLECT ITS PRESENT

BY STEPHEN H. WILDSTROM

OUT, OUT, DAMNED VIRUS

Some are benign, others can wipe out a hard disk. These programs can help

In early June, Microsoft sent 150 journalists copies of a CD-ROM demonstrating a couple of dozen programs designed by other companies to work with Microsoft Office. But the distribution was followed almost immediately by a frantic E-mail message from Microsoft's public-relations agency: Don't use the disk. It's infected with a virus. A replacement is on the way.

It just goes to show that your computer can pick up a virus just about anywhere, including from what would seem to be the most respectable sources. And the risk is getting worse. More and more software is being downloaded from the Internet. And new technologies, such as Sun Microsystems' Java and Microsoft's ActiveX, may open new channels of infection.

VECHLIKE. Just what is a virus? Strictly speaking, it is any piece of computer code that can spread from machine to machine by attaching itself to programs. Some viruses just cause inane messages, such as "Happy Birthday Yoshi," to appear on your display. Some slow down your computer or cause minor glitches. The worst can wipe out all the contents on your hard disk.

Fortunately, protecting

yourself is relatively simple. A number of antiviral products on the market will do a fine job of keeping your computer clean. I would recommend sticking with a product that's certified by the National Computer Security Assn. An up-to-date list is available on the World Wide Web at <http://www.ncsa.com>. A few choices include the Norton Anti-Virus for PCs



and Symantec Anti-Virus for Macintosh from Symantec, VirusScan from McAfee Associates, Dr Solomon's Anti-Virus Toolkit from S&S International, and F-PROT Professional from Command Software Systems. The prices range from \$45 to \$70.

All of these work in more or less the same way. When installed and at regular intervals thereafter, they scan your disk drives looking for the "signatures," characteristic strings of 1s and 0s, left by hundreds of known viruses. Between scans, they monitor every program you run,

looking for suspicious behavior, such as attempts to write to areas of your disks that contain system information. The programs differ mainly in how easy manufacturers have made it to install, set options, and update their database of virus information. Ease of use and a free update policy made Norton Anti-Virus my narrow favorite among Windows 95 products. I'm happy with the Symantec Anti-Virus I run on my Mac.

NET THREATS. Your need for good virus protection is likely to increase. For example, the virus that Microsoft accidentally sent out is a new type called a macro virus. These attach to documents, rather than programs, and could infect any machine running Microsoft Word, regardless of the operating system. The species Microsoft accidentally distributed made harmless changes in Word screens, but a more virulent strain keeps the program from saving files. Microsoft recommends general antivirus protection. But software to defend specifically against Word macro viruses is available at <http://www.microsoft.com/msword/>.

The Internet also creates new threats. Java and ActiveX work by invisibly downloading and running files on your computer, presenting an opportunity for infection every time you surf the Web. While various security measures have been designed into the systems, the bad guys are bound to find ploys that today's defenses don't address.

In all the years that I've been using computers, my machines have been infected by viruses, but I've never suffered a serious loss. I've been lucky, but I've also been vigilant. And I don't intend to relax now.

BULLETIN BOARD

ORGANIZERS

PRIME LIGHTS

If you're looking for a low-cost electronic organizer with some links to a desktop PC, consider the \$159 PS-6565SI from Texas Instruments (800 842-2737). The pocket-size organizer features excellent backlighting, which overcomes a major difficulty of many competitors: Difficulty reading in dim light. A simple desktop



cradle also makes it very easy to exchange data between the organizer and a Windows PC. Unfortunately, it works only with TI's bare-bones information-manager software. Sharing data with popular information or contact managers requires a cumbersome import and export of data.

UTILITIES

DOUBLE AGENT

It sometimes seems that the more random access memory you put in your computer, the more Windows 95 wants. Ever wonder where it goes? Agent 95 from Connectix (800 950-5880) is a \$60 utility that can tell you what applications are using the RAM. (One look at the memory consumed by Web browsers such as Netscape Navigator should persuade you to close them when not in use.) Agent 95 also helps you tune your system for optimum performance, and a RAM compression program may give you some modest performance improvement.



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Where things are

HAPPENING

BY PAUL CRAIG ROBERTS

CALL ME A JERK, BUT SOCIAL SECURITY MUST BE REFORMED



HATE MAIL:
A flood of
venom has
greeted any
criticism in
this column of
the retirement
system.
But the facts
can't be
shouted away

Over the years, my column has stimulated many readers to write in. Most letters have been complimentary, but my defenses of "junk-bond king" Michael L. Milken, "s&L crooks," and "the Reagan deficits" brought an outpouring of vitriol.

Despite the facts, many readers remain certain that Milken was convicted of insider trading. My explanation of how the 1986 Tax Reform Act collapsed commercial real estate values and, thereby, thrifts, was discounted as an apology for "the decade of greed." My assurances in the early, mid-, and late '80s that "the Reagan deficits" would not mean high inflation and high interest rates convinced many Republican readers who "knew" otherwise that supply-side economics was just another type of deficit apologetics.

But the real hate mail has been in response to my columns on Social Security. I now understand why policymakers fear to address this pressing crisis that threatens our social and economic fabric.

Most younger Americans and even some in middle age do not expect Social Security to be there for them. They have already watched the government break what former Senate Finance Committee Chairman Russell B. Long (D-La.) called the long-standing promise not to "tax a tax": Social Security benefits are subject to income tax, even though they are funded by a nondeductible tax withheld from employees' pay. This tax on benefits (85% of the benefits are taxed if the retiree has middle-class or higher retirement income) adds tax on tax.

"VICIOUS BALONEY." Social Security is well on its way to becoming a welfare system. But this is adamantly denied by the older generation, many of whom believe their benefits are paid out of an account to which they contributed over the course of their working lives. Even those who understand that the funds are commingled with general revenues believe that there is a Social Security Trust Fund containing trillions of dollars in assets.

Those who are so thoroughly misinformed naturally see me as an "outrageous liar," "a peddler of vicious baloney," "idiotic, to say the least," "a mouthpiece for a clique of Wall Street 'fat cats,'" a slanderer who seeks to destroy Franklin D. Roosevelt's creation that "keeps tens of millions of Americans from grinding poverty," and "a populist liar like Pat Buchanan."

The most striking aspect of the letters, aside from their venom, is the percentage from professionals sporting advanced degrees on their letterheads but immune to any facts about Social Security. Indeed, there is no interest in verifying or disproving my facts, only in denouncing me. "Shoot the messenger" is the time-honored attitude. Machine-gunned but not silenced, I respond with the following facts that can be checked:

Social Security is a system of intergenerational transfer payments. Those who work pay the benefits of those who are retired. When the ratio of retirees to workers rises, the benefits must be cut or the tax raised.

The Social Security tax is a payroll tax—a tax on employment. Raising the tax hurts employment, especially in an era of global competition.

The Social Security Trust Fund contains no assets except Treasury IOUs. The only way these notes can be made good is for the Treasury to borrow the money in the financial markets. In short, the Trust Fund can be paid only by deficit financing and at the expense of a larger public debt, or by massive tax increases.

POORHOUSE. According to the Social Security Trustees Report, as early as the year 2012, annual benefits will exceed revenues. Confronted with the facts, there are two choices: Policymakers can opt for a short-run solution and curtail the benefits, or raise the employment tax. Alternatively, they can begin transforming Social Security into a real pension system containing real assets in place of promises.

Officials of the American Association of Retired Persons (AARP) allege that bad investments, fraud, and Wall Street's ups and downs would relegate retirees dependent on a private pension system to the poorhouse. Even retired professors waxing fat on their Teachers Insurance & Annuity Assn. and College Retirement Equities Fund (TIAA/CREF) bond and stock pensions sometimes express this view. Of course, if the market produced such paltry and unreliable returns, life insurance companies wouldn't be able to pay off their policyholders. There would be no point to mutual funds, or pension plans, or the professional money managers overseeing the investments. Private-sector returns bear me out. Trusting the government is the foolish option.

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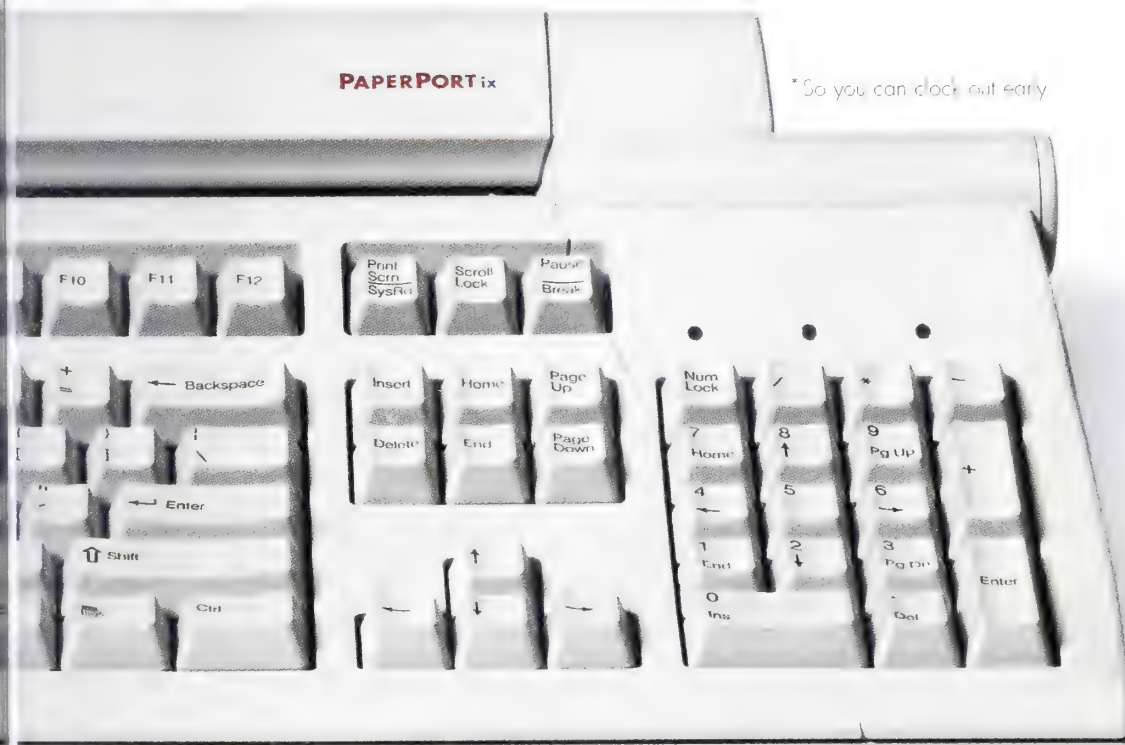


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BY HOWARD GLECKMAN

SPENDING IN THE GOLDEN YEARS

A study ties low savings to the aged

For two decades, economists have been struggling to explain the anemic U.S. savings rate. Some have blamed consumption-happy baby boomers. Many have fingered government and its intractable deficits.

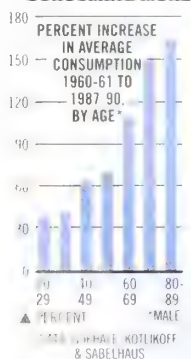
New research attributes the phenomenon to the nation's elderly. A study by Jagadeesh Gokhale of the Federal Reserve Bank of Cleveland, Laurence J. Kotlikoff of Boston University, and John E. Sabelhaus of the Congressional Budget Office traces much of the decline in national savings to two factors: a shift of resources to the elderly and a big increase in their propensity to spend—largely for health care.

In a soon-to-be-published Brookings Institution paper, the authors argue that government spending on goods and services as a share of net national product (NNP)—which adjusts national output for depreciation—has actually fallen since the 1960s. But household consumption grew from 68.8% of output in the 1960s to 76.6% by the early 1990s. The biggest contributor: Personal consumption of health care, which includes medical care financed by Medicare and Medicaid, has tripled, from 4% to almost 13% of NNP, over the past four decades.

Much of the rise in consumption, and the corresponding drop in savings rates, is a result of the redistribution of wealth from the young to the old in the form of Social Security, Medicare, and Medicaid. For example, Gokhale, Kotlikoff, and Sabelhaus figure that average consumption by men aged 70 to 79 rose by 148%

over the past three decades, adjusted for inflation, while men aged 40 to 49 showed only a 63% increase (chart). The differential for women was almost as large. As a result, note the three economists, "today's 70-year-olds are consuming, on average, roughly one-fifth more than 30-year-olds."

THE ELDERLY ARE CONSUMING MORE



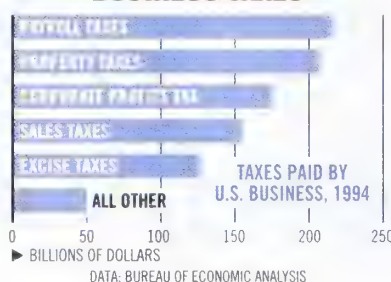
PROFIT TAXES: CRYING WOLF?

Businesses aren't really being bled

To hear the business lobby tell it, corporate income tax is the most burdensome levy on U.S. companies. Slash the tax, and American capital would be free to do wonderful things.

But the reality is quite different, according to Martin A. Sullivan of Tax Analysts, a research group in Arlington, Va. New Commerce Dept. figures crunched by Sullivan show that combined state, local, and federal taxes on corporate income are only the third-most-costly levy paid by business. In 1994, the latest year for which data is available, businesses paid \$174.9 billion

THE MOST ONEROUS BUSINESS TAXES



in corporate profits taxes. But they paid \$215.1 billion in payroll taxes and \$205.1 billion in state and local property levies. General sales taxes account for an additional \$154.4 billion. All told, profits taxes accounted for only about 18% of business tax obligations.

Put another way, corporate income taxes eat up just over 2% of gross domestic product, according to the Congressional Budget Office. Payroll taxes, by contrast, swallow 7%.

ELBOWING INTO JAPAN

Keiretsu aren't the main problem

It seems like forever that U.S. businesses and policymakers have been grumbling that foreign companies aren't able to penetrate Japanese markets. As evidence, they have pointed to Japanese government data showing that foreign companies account for only about 1% of sales in Japan.

But Harvard University economist David E. Weinstein suggests that mat-

ters may be somewhat better than conventional wisdom holds. Based on data collected by the U.S. government and by private Japanese sources, he reports that the sales figures for foreign companies total 5.7%—and could be higher. This figure, Weinstein argues, includes far more companies than do the official numbers prepared by the Ministry of International Trade & Industry.

Of course, 6% of sales doesn't exactly make for bragging rights. But here, too, Weinstein bucks conventional wisdom. He argues that the *keiretsu* system of cross-ownership by Japanese companies is not the problem. Instead, the trouble is the Japanese government's tax and regulatory policy. For instance, small and midsize companies in Japan are eligible for huge tax breaks. This discourages acquisitions by larger businesses, including foreign investors. Failure to recognize this, he insists, "has led to tremendous frustration on both sides of U.S.-Japan negotiations."

A ROSIER URBAN PICTURE

Cities are doing more with less

Despite sharp cutbacks in federal funds to local governments, the fiscal outlook for U.S. cities appears to be improving. In its annual report, the National League of Cities says most of the 381 municipalities it surveyed are maintaining service levels, and more than one-fourth are increasing services, especially for police. At the same time, the NLC says, the average general fund "carryover," or balance, which dipped in recent years to 10.5% of the general fund budget, has climbed back to an average of 14.5%—or about the same level as in the late '80s.

So how is city hall managing to do more with less? While some cities admittedly are raising taxes and other fees, a big chunk of the savings is coming from a new emphasis on boosting productivity. More than one-third of the cities that were surveyed in March and April had instituted productivity campaigns, and 29% had struck cost-sharing deals with other local bodies.

But some inequities remain between the municipal haves and have-nots: While 65% of the responding cities said they felt they could meet their fiscal needs better this year than in 1995, more than one city in four is still spending more than it collects.

By Dean Foust

Whatever happened
to the
3 martini lunch?
Heck,
whatever happened
to *lunch*?



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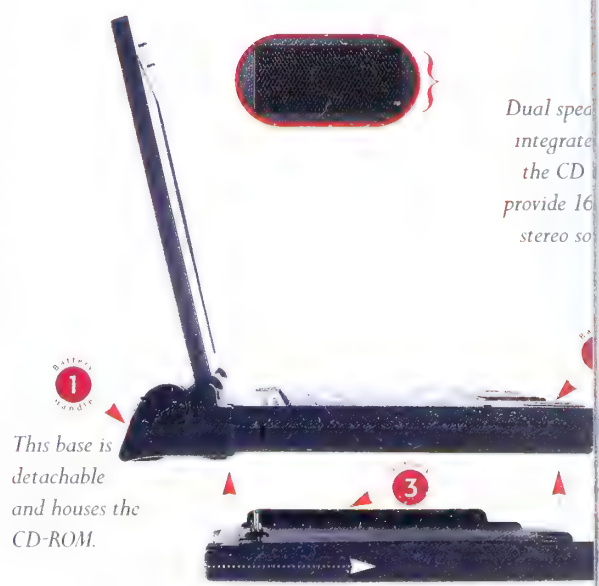
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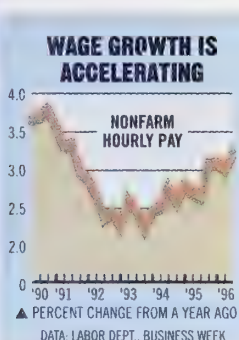
BY JAMES C. COOPER & KATHLEEN MADIGAN

WAGES: WHY THE FED HAS ITS PISTOL COCKED

U.S. ECONOMY In the megahit movie *Independence Day*, the aliens obliterate Trinity Church and its Wall Street surroundings. But on July 5, the financial markets took a real hit.

After the closing bell, Trinity was still standing, but June's surprisingly strong job-market data rocked the financial markets. The report set off inflation alarms and prompted calls for an immediate hike in interest rates by the Federal Reserve. The Dow Jones industrial average plunged 115 points on the day, and bond prices crashed, sending the yield on 30-year Treasuries to more than 7.2% at one point. Stocks have since stabilized, and the bond yield has dipped to 7.1%, but the Street remains especially edgy.

That's because the Labor Dept.'s employment report showed that for the first time in this five-year expansion, the labor markets are generating a clear inflationary threat. Jobs are growing at nearly twice the pace of the labor force, pushing the unemployment rate to a six-year low of 5.3%, a level that is already sparking a speedup in wage growth (chart).



Average hourly earnings of production workers leaped 0.8% in June, to \$11.82, the largest monthly gain in more than 12 years. Monthly data can be jumpy, but for the quarter, hourly pay rose 3.2% from a year ago, the fastest annual pace in five years. That pace has been climbing slowly but steadily for three years.

The pickup is broad-based. Manufacturing, retailing, and service industries, which make up three-fourths of private-sector jobs, have shown the most acceleration. Wages in all major categories except transportation and communications are growing faster than inflation, fueling workers' purchasing power.

THE INFLATION OUTLOOK is now at a crossroads. That's not to say that inflation is ready to spike up. But from here, the extent to which inflation rises depends greatly on wage growth. The only way that faster-rising pay will not fuel an acceleration in prices is if demand for goods and services slows—either on its own or in response to Fed tightening. And since the economy shows no sign of slowing by itself, the chances for a hike in interest rates at the Fed's Aug. 20 meeting—or possibly before—have risen sharply.

Indeed, the employment report is the strongest evi-

dence yet that the economy has the momentum to carry it beyond a simple second-quarter surge. Hours worked last quarter jumped 5.6% from the first quarter. Depending on productivity, which probably edged lower, real gross domestic product appears to have grown in the 4%-to-5% range.

The combination of fatter payrolls and bigger wage gains means that consumers generally have plenty of income. Personal income in June appears to have been a gusher, which will support spending going forward. Strong demand, especially by consumers, has thinned out inventories, fueling a pickup in factory orders and output that should last through the summer.

Factory inventories, which fell 0.2% in May, look increasingly lean. The ratio of inventories to sales is falling again. Over the past year, shipments have grown 5.7%, with inventories up only 3.1% (chart). Although factory employment dipped by 7,000 in June, the workweek rose for the third month in a row, suggesting a further gain in June output.



Also, more job gains appear to be on the way. Companies typically first lengthen their workweeks when demand picks up and then add to their payrolls if demand remains strong. In June, the overall nonfarm workweek rose by 30 minutes, to 34.7 hours, the longest in a year and a half. The increase was one of the largest on record that was not exaggerated by a temporary distortion.

THE PRICE INDEXES are still as tame as ever. But given the economy's momentum, the case that they will stay that way in the coming year—without a new round of Fed tightening—is now a lot harder to make. First, labor costs are crucial to the inflation outlook, since labor is about three-fourths of an average company's costs, and more in the case of service businesses.

What makes the wage pickup especially threatening is that it comes at a time when the economy is strong and when slack in the labor market is completely exhausted. Look at the percentage of people in the labor force working part-time because they cannot find full-time jobs. It shrank to 3.1% last quarter, the lowest since the 1970s.

At the current pace of job growth, unemployment

ERIC HOFFMANN, BW

will reach 5% by yearend, an inflationary level in any economist's notebook. Nonfarm payrolls surged by 239,000 in June, and job totals in both April and May were revised up, lifting the second-quarter pace to the highest since late 1994 (chart). That's the last year that payrolls grew faster, but for most of 1994, the jobless rate was still above 6%.

Keep an eye on unit-labor costs, too. They are inflation's prime mover. Throughout this expansion, pricing has been increasingly market-driven. That is, companies priced products according to what the market would bear, and then adjusted costs to provide profits. Now, with costs already cut to the bone, the fundamentals may be changing.

Given the gains in jobs and hours worked, productivity growth is set to slow, at least from a cyclical perspective. That means unit-labor costs will grow faster. Already, they appear to have accelerated sharply last quarter, giving businesses increased impetus to raise prices—especially amid robust demand.

AGAINST THE MOUNTING EVIDENCE, the Fed has little choice but to raise rates, especially since the financial markets are beginning to worry that Fed Chairman Alan Greenspan & Co. are falling behind the inflation-fighting curve.

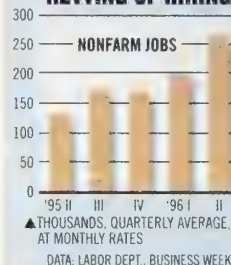
The Fed's past few beige books have mentioned spot labor shortages and wage pressures. And worries

about wage-push inflation surfaced at the Fed's May 21 meeting, according to the recently released minutes. Although the vote to leave rates unchanged was unanimous, the minutes suggest that opinion was sharply divided. Undoubtedly at the July 3 meeting, the Fed voted a formal "bias" toward tightening—the policy equivalent of a cocked gun.

Although inter-meeting shifts in policy have occurred only once since the Fed began to announce the results of its deliberations, a hike between now and the Aug. 20 meeting cannot be ruled out, especially since the period between meetings is seven weeks instead of the usual six. Such action is not Greenspan's style, because it connotes urgency. But if the financial markets think the central bank is dragging its feet, a little urgency could be justified.

In any case, the markets will be listening even more intently than usual to Greenspan's semiannual Humphrey-Hawkins testimony on July 18 for clues on the Fed's thinking. If history is any guide, Greenspan will not wait around for the alien forces of wage and price pressures to destroy his hard-won progress against inflation. He will strike first.

COMPANIES ARE REVVING UP HIRING



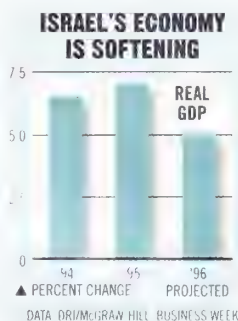
ISRAEL

A SLOWDOWN GREETS NETANYAHU

Ever since the May 29 elections that brought Benjamin Netanyahu to power, signs of an economic slowdown in Israel have been increasing.

On July 1, the Bank of Israel's index of leading indicators fell 0.7%, the first drop in 2½ years. The BOI stressed that a one-time drop, by itself, is not enough to signal trouble, but other data also point to slower growth. Tourism, for example, has been hard hit since the wave of terrorist bombings earlier this year. In addition, building starts and imports are down, and exports are stagnant. One area that is still strong is private consumption. Retail sales in May increased 2%. Real gross domestic

product jumped at a 6% annual rate in the first quarter, after a 7.1% advance in 1995 and 6.5% in 1994. For all of 1996, though, private economists expect GDP growth at a modest 5% (chart).



The rapid growth of past years triggered rises in the balance-of-payments deficit and inflation. The deficit hit a record \$4.1 billion in 1995 and is expected to reach \$5 billion this year. Inflation, which fell to a 25-year low of 8.1% in 1995, is running at nearly double that pace. Finance Minister Dan Meridor's program, adopted on July 7, is designed to deal with these two ills. The plan calls for \$1.6 billion in budget cuts over the next 18 months. The key

elements include slashing tax allowances for children, introducing user fees for medical services, hiking public transit fares, and sharply reducing grants to local and foreign direct investors.

The major impact of the government's program on the economy is not expected until 1997. Initial projections expect GDP growth to slow to 4% to 4.5%, with the unemployment rate rising to 6.5% next year, from 6% at the end of 1995.

Slower growth after a government's first year is exactly what happened when the Labor Party took over in 1992 and changed national priorities. But the economy rebounded quickly. Given Israel's high inflation and rising trade and budget deficits, the question now is how long will it take growth to bounce back.

By Neal Sandler in Jerusalem

To say it's got
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 like saying **Van Gogh**
 was pretty **good** with a can of paint.



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DRUGS

AIDS: HOPE IS WHERE THE MONEY IS



As new cases in poor nations soar, vaccine research is dwindling

In Vancouver, B.C., the 11th International Conference on AIDS was decidedly upbeat. After lean years in which new drugs were scarce but research confirming the ferocity of HIV was plentiful, an almost jubilant feeling abounded. A dozen or more reports showed that powerful combinations of drugs featuring so-called protease inhibitors are dramatically reducing the amount of virus in AIDS sufferers, raising hopes for their long-term survival.

But as promising as these drugs are, their cost—up to \$20,000 per year—renders them virtually useless for many of the 27.4 million adults afflicted with AIDS worldwide. Dr. Max Essex, chairman of the Harvard University AIDS Institute,

calls them “totally irrelevant for virtually all of the developing world.” Without an AIDS vaccine, tens of millions more will succumb to the disease—8,500 per day in industrial nations alone, according to Dr. Margaret Johnston, medical director of the International AIDS Vaccine Initiative (IAVI). “We can’t afford not to develop a vaccine,” she says.

That makes it all the more troubling that despite lofty predictions just six years ago, the near-term prospects for an effective vaccine are slim at best. The first products have proven too weak. And despite the urgent need, vaccine research is the poor step-sister to AIDS-treatment research. The National Institutes of Health spent \$1.2 billion on AIDS research last year, yet only \$112 million of that was earmarked for vaccine R&D. A report by the NIH’s Office of AIDS Research, published on July 6, found that basic research on vaccines is “vastly insufficient.”

In the developing world—where 93% of all HIV-infected people reside—vaccine research is faring even worse. Ac-

VANCOUVER RALLY: cording to Dr. The meeting’s good Seth Berkley, as- news left protesters sociate director of unimpressed health sciences at the Rockefeller

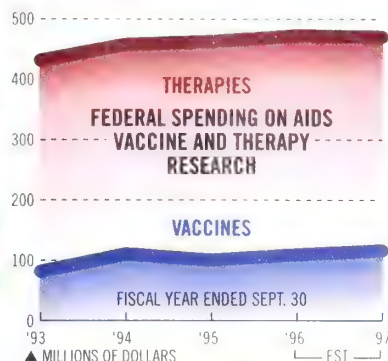
Foundation and a director of IAVI, only \$5 million of the \$10 billion spent on AIDS in developing countries goes to vaccine research. As a result, health officials from Africa and Thailand, desperate for relief, are clamoring to test any vaccines, even those that are of dubious value to their populations. For example, Genentech Inc. and Chiron

New advances are “irrelevant”

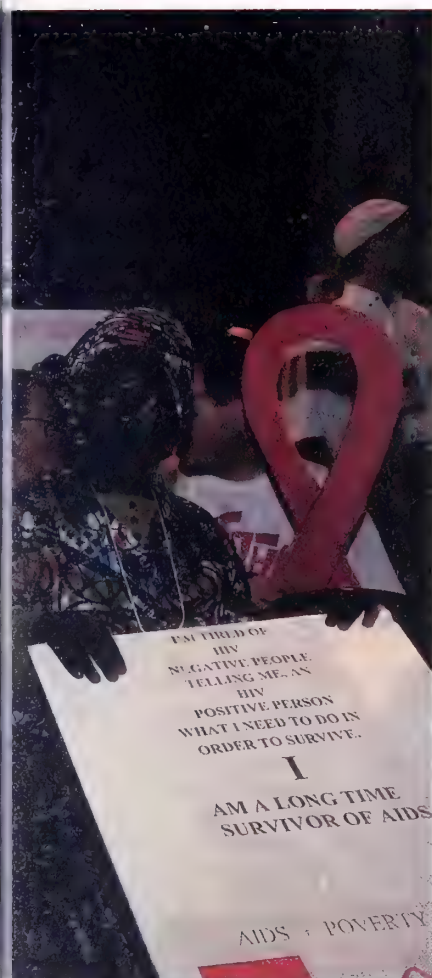
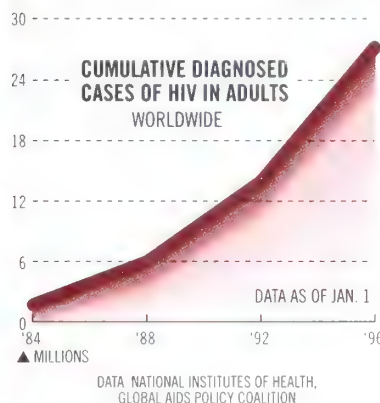
Corp. are testing products in Thailand that are not targeted at the main HIV strain found there. The Thai government hopes they may offer some protection, while the companies believe they’ll at least get some useful data on how to improve their vaccines.

Industry also has scaled back its vaccine efforts. AIDS activists have pressured companies and the government to find treatments before focusing on pre-

FOCUSING ON TREATMENT, NOT PREVENTION...



...WHILE THE RANKS OF THE NEWLY INFECTED MULTIPLY



vention. Moreover, vaccines are harder to develop than treatments, particularly without strong government support for vaccine research, so therapeutics have so far proven far more lucrative. A new report by market researcher Frost & Sullivan says that drugs for AIDS and its accompanying infections netted \$1.3 billion in 1995. And by 2000, according to a report by Montgomery Securities, prostate inhibitors could bring drugmakers an additional \$755 million in revenue. Vincent R. Zupawski Jr., CEO of Apollon

cines. At present, some 20 products are in preliminary safety trials, and just two are in small-scale clinical trials. There are no vaccines in large-scale clinical trials in the U.S.

Genentech's vaccine experience is a case in point. The company has yet to see any return on its \$100 million investment in research related to an AIDS vaccine. It is now spinning off most of a company, to be called Genenvax Inc., to do vaccine work. Company officials wouldn't comment on Genenvax because they are



virtually all

nc. in Malvern, Pa., says research "has been driven largely by the idea that therapeutic products generally will have a greater return on investment."

After more than a decade of work, only a handful of companies—including Merck in a joint venture with Vical, American Home Products in tandem with Apollon, and Genentech and Chiron on their own—are working on AIDS vac-

of the developing world"

in registration for the spin-off. But officials have said in the past that their aim is to continue to seek approval for more trials in the U.S. and Thailand.

The vaccine outlook wasn't always so bleak. In 1990, the first AIDS-vaccine product began human trials. These were so-called recombinant vaccines that contained a key protein from the outer envelope of HIV. The idea was that the

body would make antibodies that could later fight off infection.

Researchers soon discovered, however, that merely having antibodies against this protein was insufficient. Vaccines also had to incite the creation of immune-system cells that specifically recognize and destroy HIV-infected cells in the body. Without this ability, the recombinant vaccines could offer only partial protection against AIDS.

FROM "GO" TO "NO." In 1994, Dr. Anthony S. Fauci, head of the National Institute of Allergy & Infectious Diseases (NIH), concerned about the vaccines' weaknesses, decided against moving two, made by Genentech and Chiron, into large-scale trials. This move effectively stalled private-sector vaccine research, says Dr. Dino Dina, president of Chiron's vaccine business. "Within two months, we had gone from total 'go' in terms of vaccine testing to total 'no,'" he says.

The failure of the recombinant vaccines made researchers realize that the technical hurdles to preventing HIV infection are daunting. "The fundamental understanding of the biology of HIV and the immune response is so [poor], it makes trying to design a vaccine much harder," says Dr. Margaret Liu, head of Merck's DNA-based vaccine effort. Chiron's Dina compares HIV to influenza, for which a new vaccine has to be developed each year. "Here, you could argue that you need an infinite number of vaccines to protect against infection with all the possible strains."

There are indications that the search for a vaccine could revive—if the government provides some incentive. Fauci announced he's considering large-scale clinical trials of a new combination of a recombinant vaccine and a harmless virus containing HIV genes. A conference report on early human trials of Apollon's AIDS vaccine was also promising.

For the developing world, IAVI's Johnston and others believe that clinical trials of any promising vaccine should be fast-tracked. For more affluent parts of

the world, where infection rates are lower, experts are calling for companies and governments to beef up basic research and put the same intensity that yielded the current promising post-infection therapies into vaccines. In the end, only a vaccine can completely eradicate a killer.

By Naomi Freundlich in New York, with Joseph Weber in Philadelphia and John Carey in Washington

CAMPAIGN FINANCE

A DEEPENING CESSPOOL OF POLITICS AND CASH

Reform is dead, the public is numb, and anything goes

It was supposed to be a 1990s sequel to the Jimmy Stewart classic: Ms. Smith Goes to Washington. When Representative Linda Smith (R-Wash.) was elected to Congress in 1994, she vowed to clean up the cesspool of money and politics. Twenty months later, with congressional attempts at political reform collapsing and both parties carving huge new loopholes into campaign-finance laws, she has thrown up her hands. "You can't break the grip of special interests if you leave the money faucet flowing," she huffs.

Money isn't just flowing this election year—it's gushing. Experts predict record spending of more than \$1 billion on the '96 Presidential and congressional elections. Indeed, 1996 may long be remembered as the year the dam burst, with the political parties, candidates, and special-interest groups openly flouting the nation's campaign-finance laws (table). And business is among the major culprits: On July 10, a former fund-raiser for Republican Presidential candidate Bob Dole agreed to pay a record \$6 million in penalties for funneling illegal political contributions through employees of his swimming-mask company. "I've never seen anything like it," says Charles Lewis, executive director of the Center for Public Integrity, a watchdog group. "Politicians are just thumbing their noses at the law."

Much as Clinton and Dole would like to ignore it, campaign-finance reform could become a rising issue in the Presidential campaign. Former Colorado Governor Richard D. Lamm, who on July 9 announced plans to run as the candidate of Ross Perot's Reform Party, promises he will make campaign-finance

reform a top priority (box). "Our political system is broken," Lamm intoned. "If we don't fix it, we cannot begin to address the other challenges facing America."

Change isn't likely to come from inside the Beltway. The U.S. Supreme Court on June 26 made it easier for political parties to spend money at will, ruling that such expenditures constitute free speech. On Capitol Hill, efforts by Smith and other reformers have gone

ELECTION '96

HOW POLITICIANS CIRCUMVENT CAMPAIGN-FINANCE LAWS

SOFT MONEY Individuals and corporations (which otherwise are barred from direct giving to candidates) can donate unlimited funds, ostensibly for "party-building activities" such as voter registration. In reality, the money is targeted to benefit candidates.

BUNDLING Interest groups and wealthy contributors skirt the \$1,000-per-election limit on contributions to a candidate (and \$5,000 limit for political action committees) by "bundling" of checks. Often, executives send checks in the names of employees or family members.

PARTY PAYOFFS Both Presidential candidates have pushed the limits of election laws by using their national parties as piggy banks to overstep primary spending limits. The GOP has picked up travel expenses for Bob and Elizabeth Dole and put campaign officials on the party payroll. The Democratic Party has paid for TV ads hailing the successes of President Clinton.

ADVOCACY CAMPAIGNS Interest groups have spent millions on single-issue ad campaigns that often double as thinly veiled plugs for candidates. This allows tax-exempt groups such as the Christian Coalition to participate in the political process without being directly involved in partisan activity.

nowhere. The Senate couldn't muster enough votes even to consider a bipartisan effort forged by Senators John McCain (R-Ariz.) and Russell D. Feingold (D-Wis.). The House is scheduled to vote on a weak measure on July 17, but prospects for real reform are dim. "The system is out of control," says McCain.

In fact, Washington is now Loophole City. The Democratic National Committee has helped President Clinton skirt spending limits by funneling \$10 million into "issue-oriented ads" designed to benefit him without asking for direct support. And in his new book, *The*

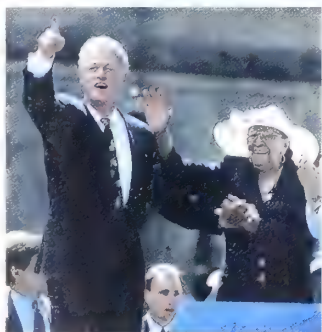
Choice, Bob Woodward alleges that Clinton himself approved and rewrote

scripts for the ad blitz blasting GOP plans to overhaul Medicare.

TOBACCO BUCKS. Dole isn't much better. After a tough primary season, he reached his legal preconvention spending limit of \$37.1 million in May. Unable to spend campaign cash until after the GOP convention on Aug. 12-16, Dole has been holding party fundraisers at many campaign stops. The result: He benefits from money that does not count toward his legal limit. "Clinton and Dole are making a mockery of the law," says Curtis B. Gans, director of the Committee for the Study of the American Electorate, a nonpartisan group.

Meanwhile, special-interest spending continues to climb. In 1995, PACs gave \$59 million to incumbents vs. \$3.6 million to challengers. Lawmakers, in turn, often feel obliged to carry water for the interest groups. Dole's critics suggest such a quid pro quo in the GOP candidate's acceptance during his career of \$477,550 from tobacco interests and his recent suggestion that cigarettes aren't always addictive.

New money games are constantly being invented. The latest: "issue-oriented advocacy," under which unions, businesses, and religious groups evade spending curbs by funneling cash, not to candidates, but into ad campaigns. Labor unions earlier this year launched a \$35 million blitz de-



signed to weaken GOP House freshmen. Business groups, led by the U.S. Chamber of Commerce, are striking back with their own ads. And groups such as the Christian Coalition are busy printing as many as 64 million voter guides—ostensibly to educate voters but in reality mainly boosting GOP candidates.

Can effective reform ever pass? In the Senate, McCain and Feingold

pushed for compromise. Candidates would get benefits such as free broadcast time and reduced postage rates in return for adhering to voluntary spending limits. The measure banned PAC contributions and required lawmakers to raise 60% of their funds in their home states. But even with the support of Clinton and Perot, these tepid measures failed.

Feingold still hopes for change. "The public disgust is rising," he says. "The next election may turn on this issue." But skeptics fret that only another Watergate-style scandal finally will force lawmakers to reject special-interest money in politics.

By Mary Beth Regan, with Stan Crock and Paul Magnusson, in Washington

CAN DICK LAMM SELL AMERICANS ON SACRIFICE?

Former Colorado Governor Richard D. Lamm, a longtime crusader for overhauling the federal budget, announced on July 9 that he would seek the Presidential nomination of Ross Perot's Reform Party, which will choose its nominee in mid-August. On June 24, Washington news editors Owen Ullmann and Douglas Harbrecht spoke with Lamm about his plans:

Q: What is your platform?

A: From the public's standpoint, I think it's [to deal with] the disillusionment and the cynicism about the political process. That's No. 1. No. 2 is that I believe I'm coming from the most fiscally irresponsible generation in American history. The federal debt is three or four times larger than we admit to when you take all the unfunded [Social Security and Medicare] liabilities that we're putting on to our children. We're going to have to talk about all the sacred cows in the budget, and that's going to be very difficult.

Q: Can you put together a winning ticket that sells pain and sacrifice?

A: I think there's a principled plurality in America that realizes we are cheating our children, that we've inherited a rich and prosperous exporting nation, and we're leaving to our children a heavily indebted importing nation. I would like to bet that you can challenge the American public to make some sacrifice.

Q: Do you worry that as a career Democrat, you might take votes away from President Clinton and throw the election to Bob Dole?

A: That's one that bothers my wife a great deal. She's very active in family planning, and she feels Dole is simply pandering to the right wing in an appalling way. It's unanswerable. You're never going to get a new broom in American



"I think there's a principled plurality in America that realizes we are cheating our children"

RICHARD LAMM
Reform Party hopeful

politics if we're controlled by that concern.

Q: Do you still feel aligned with the Democratic Party?

A: I hardly have a Democratic message anymore. I did not join the Democratic Party to transfer money from the young to the old. I can't believe we have Leona Helmsley on Medicare and 600,000 American women giving birth without adequate prenatal care. The Democratic Party is living in the afterglow of the New Deal and is absolutely irresponsible in terms of coming up with the kind of vision needed in the future.

Q: Do you actually think you can win a three-way race?

A: The Republicans are having such a difficult time as a party, and there are enough Democrats who understand that the New Deal has become a raw deal for our kids. I'm not scheduling Camp David yet. But if I lose, I win—if I can do this with honor. Ross Perot performed an im-

mense function in 1992, waking up the nation. I believe truly that America needs a realistic agenda.

Q: Where do you stand on abortion? Are you pro-choice?

A: I was the sponsor of the nation's first liberalized abortion law.

Q: Your view on affirmative action?

A: I would restrict affirmative action to 10 more years and make it apply to only native-born blacks and Hispanics. I don't see inviting someone into your country and then giving them your job.

Q: Do you think some of your past embarrassments could hurt you politically? There was a flap when you were governor over your dealings with a Denver stockbroker who was later convicted on federal racketeering charges.

A: That will undoubtedly be a problem. I gave \$5,000 to the guy I used to practice law with, and he invested it [with the stockbroker] and did very well. That thing has been investigated by an ethics committee, which found really nothing wrong with it. Also by the U.S. Attorney, who found nothing wrong with it, and the Securities & Exchange Commission. But I think there was something wrong with it. I was at fault: I should have been monitoring what he was doing better.

Q: How much did you make?

A: I've really repressed it. I think it's in the neighborhood of \$40,000 [which he says he gave to charity].

Q: Other controversies in your past?

A: I've said we can't retire people from the military at 42; we don't need 175 Veterans Administration hospitals. I've taken on every sacred cow in the book. My hard-choice agenda is certainly beyond the ordinary in politics.

EXECUTIVE SUITE

WILL GRAY HAIR BE AN ASSET TO APPLE?

Amelio's SWAT team has plenty of experience—but not in PCs

The old saw about Apple Computer Inc. needing some adult supervision can now be shelved. On July 3, Chief Executive Gilbert F. Amelio added the final member to his senior management team: Ellen M. Hancock, the 53-year-old former IBM and National Semiconductor Corp. exec who will be Apple's chief technology officer. With her hiring, Amelio, in his job since February, has assembled a five-person executive staff at Apple's Cupertino (Calif.) headquarters, with some 140 years of combined high-tech experience.

Trouble is, none of that experience is in the PC business. That has experts questioning whether Amelio's team has what it takes to reverse Apple's dwindling fortunes at a critical juncture. Five months into Amelio's tenure, Apple sales are slipping badly in key markets. Home Mac sales are down as much as 30%, say some retailers, and even suppliers in Mac hotspots such as publishing report no growth. On July 17, the computer maker is expected to report its third straight quarterly loss, which Montgomery Securities analyst Kurtis King estimates at \$204 million.

Apple has said to expect losses for now, but investors are deeply unhappy. Shares are trading at a 10-year low of 19, down from 30 when he arrived, and there are revived press reports of a sale of part or all of the company. Says Standard & Poor's Corp. analyst Molly Toll-Reed: "If there's no progress in six months, you'll have to question the whole management strategy."

The executive team insists that Apple's predicament is nothing some management discipline can't fix. "It'll take three years to return the company to a success model, but I believe we'll see gradual improvement from here on in," says Chief Financial Officer Fred Anderson. Among the changes in the offing: Apple is recruiting two new directors, and company co-founder A.C.

That means the top team needs to bone up now on the ins and outs of the PC business. And some of Apple's newcomers have a decidedly mixed employment record. Anderson helped manage minicomputer maker MAI Systems Corp. through the PC revolution. But Scalise was bumped from Maxtor Corp. in 1991 amid mounting losses. And Hancock went to National after being passed up for a top software job by IBM boss Louis V. Gerstner Jr. One mistake: backing an IBM technology instead of jumping on the Internet bandwagon. Hancock says she was late to grasp the significance of the Internet, but adds: "I'm very supportive of a strong Internet play now."

Much of the immediate work that needs to be done will fall to Landi, a 1995 arrival from chipmaker Texas In-

THE TOP BANANAS AT APPLE

Since joining Apple as CEO in February, Gilbert Amelio has built a management team populated heavily by National Semi veterans.

FRED ANDERSON (51)

Chief financial officer

The former CFO at ADP, he has staved off a cash crunch—for now. **1996 PAY:** \$900,000, plus an \$800,000 signing bonus and options now worth \$4.7 million.

ELLEN HANCOCK (53)

Chief technical officer

Once IBM's top female executive, she later joined National. She left the chipmaker in mid-April when she wasn't named to replace Amelio. **1996 PAY:** Undisclosed.

GEORGE SCALISE (61)

Chief administrative officer

Amelio's right-hand man at National, he led a short-lived revival at Maxtor. **1996 PAY:** \$735,000, plus a \$630,000 signing bonus and \$3.2 million in options.

DATA: BUSINESS WEEK, PEARL MEYER & PARTNERS



ON THE CASE: Amelio (left), with Anderson, Hancock, and Scalise



MARCO LANDI (52)

Chief operating officer

A 25-year veteran of Texas Instruments, he revamped Apple Europe in 1994. Now, he has to fix Apple's dysfunctional sales organization.

1996 PAY: Undisclosed.

"Mike" Markkula is expecting to leave the board, according to one source. Insiders deny that Apple needs to sell off chunks of the business. "The reason we would sell a business is to raise cash, but we have a healthy balance sheet right now," says one of Amelio's direct reports. Still, the executives are staring a deadline in the face: The company's stated goal is to return Apple to profitability by next March.

struments Inc. who headed Apple Europe before Amelio promoted him to COO in May. His mission: to mend fences with customers and partners, irked by Apple's arrogance. He already has met with more than 150 of them. He is also trying to bring out a new collection of Macs this fall and has begun to put PowerBooks back on retailers' shelves—left empty for 60-plus days, distributors say, after a May recall. Landi also is

putting in motion a key element of Amelio's restructuring plan, announced on May 14: cutting in half the number of Mac models by mid-1997.

Will these moves be enough? Not even close, say experts. The only sure-fire solution to Apple's woes lies in innovative technology. That's Hancock's mandate. And on July 9, just 36 hours into her new job, the 29-year IBM vet-

eran met with key staffers to discuss how to light a fire under Apple's coddled software engineers, who have been struggling for years to deliver Apple's new Mac operating system, dubbed Copland. "We have a lot of 25-year-old wizards around here," says Hancock. "My skill is getting things to market."

Well, maybe. Critics say IBM missed the boom in networking gear because

Hancock failed to deliver on a key product. And she's known more as a buttoned-down manager than as a visionary. While experience counts in Silicon Valley, "the complexity when you come to Cupertino increases exponentially," says one Apple manager. Apple's new team will have to master the new math.

By Peter Burrows in Cupertino

STRATEGIES

WHY MOTOROLA HAS NONWORKING NUMBERS

Tough competition in cellular and chips yields a sorry quarter

The news was the sort of shock that Wall Street despises. On July 9, Motorola Inc. announced that it had earned \$326 million, or 54¢ a share, in its second quarter—well below estimates of 68¢. To Wall Street's way of thinking, that was a major rout. Just the day before, a Cowen & Co. analyst had put a "strong buy" on the company. Motorola's punishment was severe: The company's stock tumbled nearly 8% points, or 13%, to 57¢ on the news.

The earnings shortfall and investor dismay pose a major challenge for Motorola Chief Executive Gary L. Tooker, who took the helm at Motorola in 1993. In the face of stiff competition from rivals, the company has adopted a take-no-prisoners competitive strategy that is likely to keep results under pressure throughout the year. **TURN OF THE SCREW.** Take the cellular-phone business. With new rivals driving down prices, Motorola aims to hold on to its position as the world's top cell-phone provider—whatever the cost. "We're not going to let competitors come in and take market share," vows James P. Caile, vice-president of marketing for Motorola's cellular subscriber group.

But Motorola will have to spend heavily to defend its turf. Competitors Nokia Group and L. M. Ericsson have improved the quality and design of their products. Then there's the price war problem. Cellular operators, who purchase phones made by Motorola and its rivals and then sell or give them to their customers, have been turning the screws

on equipment providers. As a result, the average wholesale price of a cellular phone has been cut in half over the last three years, to about \$175. Some Motorola models, such as the tiny StarTAC, introduced earlier this year, command top dollar. But no premium lasts long in the current price wars.

The pricing pressure won't lift soon. Operators, such as AT&T's wireless division, are having to spend heavily to acquire new customers—just as those customers are using their phones less. That and declining prices have sliced the average monthly cellular bill in half over the past eight years, to \$51 a month, according to the Cellular Telecommunications Industry Assn. "There's significant pressure from operators to lower

the wholesale price of phones—and Motorola is definitely feeling that," says Mark J. Lowenstein, vice-president of wireless communications research at the Yankee Group.

Contributing to the softer pricing is a slowdown in the growth of the cellular market. The number of U.S. subscribers has been increasing by about 30% annually, but some analysts expect the rate to drop to about 10% this year. "There's just very little demand," says Bear Stearns & Co. analyst Alex Cena. Outside the U.S., growth will be stronger. Worldwide, the rate of expansion among cellular-phone subscribers is expected to slow only modestly from the 35% annual rate of recent years.

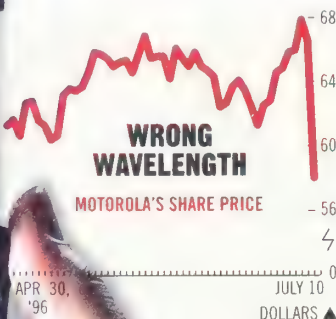
CHIP SQUEEZE. Motorola's semiconductor group has been caught in a similar squeeze. After the industry grew 42% last year, the company expects growth to decline by as much as 10% in 1996. A large part of the drop has occurred in the memory-chip business, where Motorola has only a minor presence. Still, Motorola faces soft demand from its own communications business and from Apple Computer Inc., a major buyer of its PowerPC processors.

Tooker's main challenge now: finding new sources of growth. Motorola is hoping that personal communications services (PCS), a new kind of wireless technology, will help turn around its fortunes in 1997. With a spate of new operators receiving PCS licenses across the U.S., Motorola expects wireless-telephone usage to increase dramatically. Caile says it's realistic to expect the number of wireless phone users to triple worldwide over the next five years, to 300 million. "I'm personally very bullish on the long term," says Caile.

Even in this new technology, though, Motorola will have to fight hard for its position. A recent Yankee Group study said the company holds just a 12% share of the U.S. market for PCS infrastructure equipment, well below its 20% share of the cellular market.

Motorola vows to keep its 40% share of the wireless-telephone market—no matter what the cost. It's a strategy that means Tooker will remain in the hot seat, as Wall Street warily watches Motorola's bottom line.

By Peter Elstrom in Chicago



DATA: BLOOMBERG FINANCIAL MARKETS

CELLULAR RIVALS ARE DRIVING DOWN PRICES

STRATEGIES

PUTTING THE SNAP BACK IN SNAPPLE

Parent Quaker Oats must boost sales or a restructuring looms



The strategy is so simple, it's surprising that Quaker Oats Co. didn't think of it sooner: Can't sell enough Snapple? Give it away.

It's no joke—at least not yet. A big giveaway is at the center of Quaker's latest effort to revive its faltering Snapple brand. From mid-July through mid-September, Quaker will spend up to \$40 million handing out 16-ounce bottles of its iced teas and fruit drinks to all comers, "spreading taste all over the place," as its new TV and radio ads will say. The plan calls for "sampling brigades" to pass out free Snapple nationwide, at beaches, parks, and on street corners. Consumers also can call a toll-free number to get coupons good for free bottles.

FIREWORKS. Snapple could use extra juice. Sales are up only a fraction the first half of the year, experts figure, while Quaker's Gatorade beverages are up nearly 10%. Quaker CEO William D. Smithburg terms the marketing push a prudent investment in Snapple's potential: "I'm more interested in getting the momentum and sales up than I am in maximizing short-term profit," he says.

But for Smithburg, who bet the farm on his Snapple acquisition, this latest show of marketing fireworks could be a grand finale. If it fizzles, watch for a write-down. Quaker anted up \$1.7 billion for Snapple and assumed its debt—then booked a punishing \$1.8 billion in good-

will on the purchase. Beyond that, if Snapple still lags, a restructuring of Quaker may be in the offing. The most likely scenario: A spin-off of the company's \$2 billion drink business under the Gatorade name. Smithburg concedes a spin-off is a possibility, though he says he's not yet convinced his beverage and food units would be better run apart.

A spin-off would give greater visibility to Gatorade. Just a few years ago, Quaker's sports-drink business seemed on the brink of disaster as Coca-Cola Co. and PepsiCo Inc. rolled out competing products. Today, Gatorade's market-share has stabilized at a dominant 80% and Coke's Powerade and Pepsi All Sport are battling for the distant No.2 spot. Boasts Sue Wellington, Gatorade marketing vice-president: "We are kicking ass and taking

names." How so? Gatorade has become a fixture at sports events, scored points with new flavors and packaging, and signed up a slam-dunk spokesman in basketball star Michael Jordan.

POOR SHOWING. For the moment, Quaker has little else to brag about. The price war in cereals will shave as much as \$40 million off its earnings this year. Other brands such as Quaker Oatmeal and Rice-A-Roni are up, but only in comparison with a dismal first half in 1995. As for Snapple, Quaker announced on June 26 that it expects the business to post a loss this year because of Smithburg's extra marketing push.

GIVEAWAYS

Quaker will spend up to \$40 million handing out free iced teas and fruit drinks through September

As a result, Quaker's earnings from continuing operations will hit \$175.4 million this year on sales that will be flat at \$5.4 billion, figures Prudential Securities Inc. analyst John M. McMillin. Those earnings would be up 76% from last year's poor showing but well below the \$305 million posted in pre-

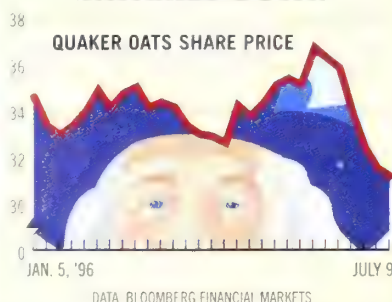
September 1993. The outlook knocked Quaker's stock down 15%, to 31¼ from June 25 to July 9 (chart). "They're not on the right track," says analyst Arthur Cecil of T. Rowe Price Associates Inc., which holds about 2 million shares.

Part of the trouble has been Smithburg's optimism. At an analysts' confab in February, skeptics dubbed his forecast of 15% to 20% gains in Snapple sales this season "gulp fiction." The skeptics were right: Ads positioning the brand as an underdog alternative to Coke and Pepsi fell flat, and Quaker dumped longtime agency Kirshenbaum Bond & Partners. Now, Foote, Cone & Belding, the new agency, has a tall order to fill in cobbling together a campaign in midsummer. "They're trying to turn it around at the 11th hour. They desperately need this marketing blitz to be successful," says Goldman, Sachs & Co. analyst Nomi Ghez.

Quaker stock might trade even lower, analysts say, if it weren't for spin-off rumors. That's because Gatorade, even combined with slower-growth Snapple, would likely command a higher valuation as a "pure" beverage play. A spin-off also could free up the beverage and food businesses. "The board has got to start seriously addressing a spin-off," insists McMillin. If Smithburg's big giveaway doesn't work, maybe it will.

By Greg Burns in Chicago

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ICE BATH
A microscopic embryo like the unfrozen four-cell one above is frozen at NYU Medical Center

CONTROVERSIES

A DELICATE ISSUE FROZEN IN TIME

What to do with thousands of embryos that will never be used

On July 31, a peculiar ritual will be performed at the Bourn Hall Clinic in Cambridge, England, where the world's first test-tube baby was born 18 years ago. White-coated laboratory technicians will gently lift metal cylinders containing roughly a thousand frozen human embryos from frosty baths of liquid nitrogen. Tiny glass ampules with embryos of up to eight cells will be placed in a bath of warm water, where they will be allowed to get too warm—and die. "The official jargon is 'we will interfere with the thawing process,'" says Susan M. Avery, Bourn Hall's scientific director.

The destruction is mandated by a British law that says frozen embryos must be discarded after five years, a countdown that began when the law took effect on Aug. 1, 1991. Now, as time runs out, fertility clinics across Britain also are preparing to destroy thousands of embryos. That highlights a question that faces many other nations, including the U.S.: What should be done with the thousands of embryos, created through test-tube fertilization, that have been forgotten or might never be used?

It's more than an academic question for Americans. There are some 20,000

unclaimed embryos in U.S. clinics, says Arthur Caplan, director of the Center for Bioethics at the University of Pennsylvania. The reason: When women seek help from in-vitro fertilization (IVF) clinics, doctors may fertilize a dozen eggs to increase the chances of success. Some are implanted; the rest are frozen. Years later, clinics may lose touch with some of the couples that produced them, and storage fees may go unpaid. That leaves the embryos suspended in a timeless, ice-cold ethical and legal morass.

ABORTION DEBATE. Unlike Britain, moreover, the U.S. has no regulations to cover the disposition of the embryos. "Our stance," says Caplan, "has been to solve the moral dilemma by doing nothing." Caplan argues that Britain's approach is "a sound one." But most experts don't think it would work in the U.S., where the question of what to do with unclaimed embryos gets caught up in the emotional abortion debate.

Most scientists don't see any easy way to end the ethical gridlock over embryo regulation in the U.S. Ronald M. Green, director of the Institute for the Study of Applied & Professional Ethics at Dartmouth College, says any attempt to deal with the problem "is

likely to rekindle a bitter controversy." Green has been knocked down before: He was a member of a national panel

that recommended federal funding for embryo research. Many say that's the best way to learn about chromosome abnormalities in the earliest stages of human development. Congress' reaction to the panel's counsel was decisive: Earlier this year, under pressure from religious conservatives, it banned federal funding for such research.

U.S. clinics have tried to deal with the issue. Many now ask couples to sign con-

sent forms that include specifying when embryos can be discarded, who gets custody in a divorce, and whether they can be used for research. Such precautions, says Dr. Jamie Grifo, director of the infertility clinic at New York University Medical Center, avoid "a lot of the problems of having embryos you don't know what to do with."

FIVE MORE YEARS. Even legal mandates, however, don't resolve all the moral dilemmas inherent in destroying human embryos. Britain is finding that out. Susan Avery and her colleagues at Bourn Hall threatened to defy the embryo law when it was first passed. In May, the law was amended to allow parents to request that their embryos be preserved for five more years. Bourn Hall struggled to reach every donor couple, but the clinic failed to find 250 couples with 1,000 embryos in storage. These embryos must be destroyed. But Avery worries that some people, mistakenly believing their embryos would be stored indefinitely, may later turn up to demand them. "That's an intolerable situation," she says.

Even for those who have no moral objection to destroying embryos, an Orwellian scent lingers over the proceedings. "People of all perspectives realize that we're dealing with something that is very symbolic to us of the sanctity of human life," says Green. Avery takes solace in the fact that fertility clinics have contributed to the birth of thousands of children who otherwise might never have been born. But with that blessing comes an ethical conundrum that may never be completely solved.

By Paul Raeburn in New York

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COMMENTARY

By Keith H. Hammonds

HOW TO PUMP MORE LIFE INTO AMERICA'S CITIES

It is a heady, expensive quest for urban rebirth. Since 1991, Cleveland has sparked construction of more than 2,000 homes by committing \$20.3 million to a \$120 million loan fund and offering property tax abatements of 10 to 15 years. Homes priced at \$150,000 and up have sprouted in Hough and Fairfax, gritty inner-city neighborhoods. Retail development is helping to lure new middle-class residents from the 'burbs.

All that, and Cleveland's population, at around 500,000, hasn't budged in five years—far better than the scary exodus the city suffered in the decade before, but also far from robust. That's no surprise: Across the U.S., urban flight still prevails. While 1995 data on private-sector lending, due out in late July, likely will show an expansion of mortgage lending in underserved neighborhoods, the proportion of housing permits accounted for by inner cities continues to skid (chart). "More money is going into urban areas, but not enough to turn the tide of money leaking out," says Nancy McArdle, co-author of a recent report from Harvard's Joint Center for Housing Studies.

VOUCHER PLANS. Urban rot, though, isn't inexorable. In small pockets of America's cities, communities are building solid housing and better schools, funded by innovative public-private partnerships. Retail and commercial projects, such as the Pathmark Stores Inc. outlet set to open in New York's East Harlem in 1998, are sinking crucial roots for economic stability. "These are not sizable enough to show up in national statistics," says G. Thomas Kingsley, director of the Urban Institute's Public Finance & Housing Center. "But they're nonetheless important because they're happening in places where a few years ago, people thought nothing would happen."



HOOP DREAMS: New housing credits could slow urban flight 'burbs.

A rethinking of public policy can help replicate and expand these small victories. For starters, the feds must dismantle housing strategies that for years have roped off the urban poor in flimsy apartment complexes. To his credit, Housing & Urban Development Secretary Henry G. Cisneros is attempting just that: HUD is tearing down hundreds of failed high-rise apartment buildings, replacing them with mixed-income housing that can retain a core of middle-class professional residents. Chicago has targeted its infamous Cabrini Green complex for such an overhaul.

Cisneros wants to go further, providing vouchers that would allow project tenants to rent better homes elsewhere in the city. Congressional Republicans killed off this sweeping market-based plan—which could have saved at least \$640 million a

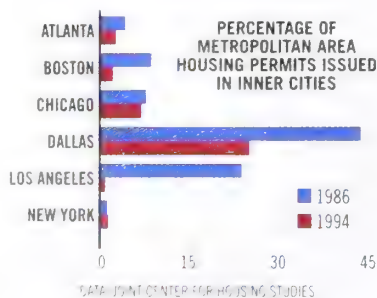
year—but returned this year with a more cautious voucher system of their own. Not perfect, but not bad.

The U.S. should also expand the federal Low-Income Housing Tax Credit. Under the \$3.3 billion program, which survived the budget-slashers' attack this year, syndicators and community groups direct corporate dollars into 100,000 units of affordable housing a year, literally transforming hundreds of blocks in Newark, Kansas City, and elsewhere. But the level of congressional authorization for the program hasn't changed since 1986. Because of a quirk in allocation, moreover, availability of the credits is shrinking even as demand from developers intensifies.

LEVEL THE FIELD. The most compelling answer to urban flight, though, remains the most contentious. The home mortgage deduction is by far the federal government's biggest housing subsidy, worth \$58 billion in 1995. Yet it's worthless to many low- and middle-income taxpayers, who are unlikely to pay mortgage interest greater than the standard family deduction of \$6,550 a year. That leaves such families, many of them urbanites, with little fiscal incentive to buy a home, while the wealthiest 5% of Americans pocket close to half of all mortgage deductions.

Occidental College Professor Peter Dreier, a former Boston housing commissioner, argues for a progressive mortgage tax credit that provides equivalent benefits to all home buyers. That would at least level the playing field. Then build some good homes, bring in jobs, rehabilitate schools, and people might actually want to live in urban neighborhoods. Until then, cities must content themselves with modest successes, block by block.

DOWNTOWN DOWNTURN



Hammonds covers social issues for BUSINESS WEEK.

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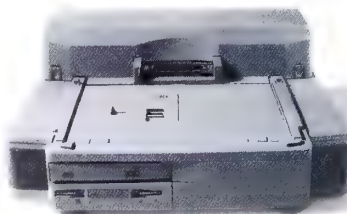
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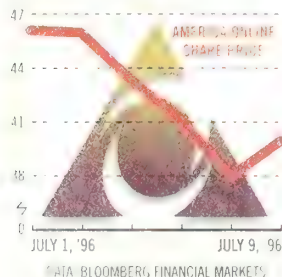
VALUJET: FLYING SMALLER?

IF VALUJET AIRLINES EVER does get off the ground again, it won't have the clear flight path it enjoyed when it began operations in late 1993. The carrier, which said in a Federal Aviation Administration filing that it hopes to resume service in August, will be limited to 15 planes, fewer than a third of its fleet before the fatal May 11 crash of Flight 592, in which 110 people died. Costs will be higher, because ValuJet is taking most maintenance operations in-house rather than contracting them out. And its chief competitor, Delta Air Lines, is leaner and meaner after a two-year cost-cutting program. ValuJet officials won't say whether they'll

CLOSING BELL

BACK ONLINE

Rough ride for America Online: Its stock took a pounding on July 8, dropping from 41½ to 38 on news that AOL had reached a tentative settlement in 11 class actions over its pricing practices. The deal, which needs court approval, requires AOL to offer free hours of service or pay the dollar value of those hours to current and former members. But a closer look at the terms encouraged investors, who pushed AOL to 40 on July 9: Estimates put the deal's costs for AOL at just \$10 million.



push into newer markets, such as New York, or simply fall back on the routes to Florida on which the airline's business was founded.

SUDDENLY, HUMANA IS HEIRLESS

NOT EXACTLY A SIGN OF health: Wayne Smith, president, chief operating officer, and likely heir to founder David Jones at health insurer Humana, abruptly retired on July 10. Jones, 64, had been expecting to retire at yearend, but he will now stay on. Humana refused to explain Smith's departure, and Smith couldn't be reached. The company named Gregory Wolf, its senior vice-president for sales and marketing, as chief operating officer. Humana stunned investors a month ago when it said second-quarter earnings would decline up to 36% from a year earlier partly because of customers' higher-than-expected usage of medical services.

NIKE JUST KEEPS GOING AND GOING...

NIKE JUST DID IT—AGAIN. THE company blew past even the most optimistic analysts' projections on July 9, reporting record earnings. Much of the success is the result of expansion in Europe and Asia, plus phenomenal increases in its new apparel line. In the U.S. alone, apparel revenues grew 99% for the fiscal year. For most, that kind of growth is tough to sustain. But Nike reported that future worldwide orders for footwear and apparel are 55% higher than the past year's, signaling that its winning streak is far from over.

TIME WARNER-TURNER'S NEMESIS

TIME WARNER'S PROPOSED \$7.5 billion merger with Turner Broadcasting System is in for

HEADLINER: MICHAEL PRICE

IN A LATHER OVER DIAL

He's at it again. Michael Price, chairman of mutual-fund company Heine Securities, has successfully agitated for change at companies as large as Chase Manhattan. Now, he's taking on Dial, criticizing the company's plan to split in two.

Price's charges, contained in a July 8 Securities & Exchange Commission filing, come just weeks after he agreed to sell Heine to Franklin Resources for up to \$800 million. Apparently, that hasn't slowed him down. Price declined to comment.

In Dial's plan, announced on Feb. 15, the "new Dial" would concentrate on con-

sumer products while the second company, Viad, would own and operate service businesses. That's not enough, says Price, whose funds control 9.9% of the stock. He says Dial should realize up to \$330 million by selling assets such as executive jets and corporate residences, and he plans to confer with other shareholders, raising the specter of a proxy fight. Dial says the company has already sold a plane and is considering other asset sales.

Price has reason to be unhappy: His funds bought Dial shares at an average price of 29. It's now at 28%.
By Jeffrey Laderman



a difficult time now that the Federal Trade Commission's staff has recommended that the agency not approve the proposed deal. The staff believes the combined company—along with cable giant Tele-Communications, which owns roughly 20% of Turner Broadcasting—could squash competitors in both cable-television systems and programming. The FTC may vote on the deal as early as mid-July and will likely pay serious attention to the staff analysis. But the companies insist the deal could still go through.

THREE CHERRIES FOR SIX FLAGS?

MOVE OVER, MICKEY. SIX Flags Theme Parks plans to build a new \$200 million park in Connecticut that could be bigger than Disneyland. The location: just down the road from the Foxwoods casino in

North Stonington, Conn., which is owned by the Mashantucket Pequot tribe and is said to be the most profitable in the world. The new park could add to the 12,000 or so guests at the casino every day. Six Flags will lease the land for the park from the tribe, which is looking for ways to spend the billions it earns from Foxwoods. The tribe is already building a ferry to shuttle visitors to the casino from New York and Boston.

ET CETERA...

- Royal Dutch/Shell and Exxon are combining their petroleum-additives businesses.
- Pepsi's Christopher Sinclair, head of its beverage business, abruptly resigned.
- Procter & Gamble is repurchasing up to \$1 billion in stock.
- Infiniti ranks first in customer satisfaction in the J. D. Power survey.

WE INTERRUPT THIS REVOLUTION TO HIKE THE MINIMUM WAGE

Republican firebrands stormed Capitol Hill in 1995 vowing to bury the Welfare State. Yet as the 104th Congress limps toward a close, GOP lawmakers find themselves poised to enact a Democratic plan that passed the Senate on July 9 to boost the minimum wage. It's a powerful sign of how far off track the once vaunted Republican Revolution has strayed. And it shows how scared many GOP incumbents are of the "extremist" label pinned on them by the opposition.

By now, the GOP had hoped, it would have realized its grand plan to remake government, an achievement that would have strengthened its grip on Congress this fall. Instead, Republicans have fallen far short of their expectations—and are in jeopardy of losing their hold on the House.

That has Hill Republicans scrambling. Some first-termers are distancing themselves from the polarizing leader of the revolution, House Speaker Newt Gingrich (R-Ga.). Meanwhile, the leadership is launching a communications counteroffensive to convince voters that the first Republican Congress in 40 years has been far more successful—and mainstream—than critics contend. House Majority Leader Richard K. Arney of Texas and Representative John A. Boehner of Ohio, the House Republican Conference chairman, have given incumbents a 122-page inventory listing nearly 1,000 achievements of this Congress.

OMINOUS POLL. The strategy: deflect attention from their shortcomings by boasting that they've begun dismantling Big Government. Indeed, the GOP cut discretionary spending for the first time since 1969 and scrapped more than 270 programs or agencies. The party will also remind voters that it passed historic reforms of telecommunications regulation and farm programs, overhauled lobbying laws for the first time in 50 years, and adopted strict curbs on accepting gifts. The list would be longer had President Clinton not vetoed such

GOP measures as tax cuts, welfare overhaul, and legal reform.

Still, Gingrich's troops have enacted only 3 of the 10 tenets of their Contract With America, failing to deliver a balanced-budget amendment, term limits, and sweeping deregulation. Moreover, Democrats have stirred up voters against things the GOP tried but failed to do—overhaul Medicare, end the Medicaid entitlement, and roll back environmental regulations.

Which view of the 104th will the public believe: mainstream success or extremist failure? So far, Democrats are winning the

PR war. Polls show voters prefer House Democrats over Republicans by up to 9%—a margin not seen in four years. More ominous for the GOP, Congress' job-approval rating was an anemic 19%, according to a June CBS/*New York Times* poll. Gloats Clinton campaign spokesman Joe Lockhart: "They promised a lot and delivered very little."

Republicans blame their image woes on liberal media bias, an ad blitz by organized labor, and their own inability to sell their successes. "We've had a mainstream agenda of tax relief and returning power to the people, but it has been mischaracterized by the Administration and some elements of the national media," gripes National Republican Congressional Committee Chairman Bill Paxon (R-N. Y.).

But analysts say the GOP's ills run deeper than poor communications. Says James Thurber, director of the Center for Congressional & Presidential Studies at American University in Washington: "Voters aren't nearly as radical as some [Republicans] who were elected."

That's why many endangered Republicans are trying to shed their hard-right reputation by voting to raise the minimum wage. A betrayal of the revolution? Perhaps, but it may be the only way for the party that ran the 104th Congress to keep its hold on the 105th.

By Richard S. Dunham



ARNEY: PR counteroffensive

CAPITAL WRAPUP

NET SCRAPE WITH THE FCC

► Federal Communications Commission Chairman Reed E. Hundt has some Internet interests fretting. In a recent speech, Hundt's chief of staff raised the possibility that Internet providers may eventually lose their exemption from access charges that long-distance companies pay to connect to local phone networks. While the charges should come down under the new telecommunications law, Internet execs are flocking to the FCC to persuade staffers to dump the idea.

THE SPEAKER'S SAFE SEAT

► Democrats thought they had a strong challenger for House Speaker Newt Gingrich's suburban Atlanta seat: cookie tycoon Michael J. Coles, chief executive of Great American Cookie Co. But despite millionaire Coles's deep pockets, an internal Gingrich poll shows the Speaker way ahead, 62% to 20%. That means Newt won't be tied down campaigning in his home district, and will be free to stump for other Republican candidates nationwide.

A BITTER PILL FOR DRUGGISTS

► The Food & Drug Administration figured its proposal that pharmacists include more information with prescriptions on how to take medicine would save up to \$1 billion a year in reduced hospital admissions. But the National Association of Chain Drug Stores gagged on the idea. Its argument that many pharmacies voluntarily dispense extra information has convinced Senator Thad Cochran (R-Miss.), who chairs the panel that funds the FDA, to block any spending for the rule.

RUSSIA

THE NEW TROIKA IN MOSCOW

A tug-of-war between Yeltsin's henchmen won't derail reform

The jockeying for position was obvious. In the two weeks leading up to Russia's July 3 presidential election, voters saw even more of retired General Alexander Lebed than they did of his campaign partner, candidate Boris Yeltsin. Lebed's gruff voice boomed from TV screens across the country. His pug-nosed face peered out of every newspaper. But the day after Yeltsin beat his communist rival by a 53.8%-to-40.3% margin, it was Prime Minister Viktor Chernomyrdin who appeared before the cameras to trumpet Yeltsin's new programs.

Tired and ailing, Yeltsin is quickly delegating power to his two comrades in the new troika. Lebed and Chernomyrdin are already fighting over turf, and both think they deserve to be Yeltsin's successor. Yet despite the power struggle inside the Kremlin, Yeltsin's decisive win marks a turning point. After enduring five years of economic chaos, Russian voters have resoundingly rejected a return to the Soviet system. Instead, they are gambling on the free market, with its volatility and risks as well as its rewards. Russians were no doubt voting as much against communism as for Yeltsin himself. But the outcome is the same: There's no turning back from the reforms he began.

SHIFTING BALANCE. After a first term devoted largely to stabilizing inflation and taming the wild seesaws of the ruble, the new Yeltsin team is geared up to promote all-out growth. By the end of Yeltsin's second term at the turn of the century, he wants to set Russia on a

course toward full membership in the developed industrial world. That will mean bringing the nation closer to Western business practices, attracting more portfolio and direct investment, and imposing discipline on the "Wild East" culture that has hampered growth. At the same time, Yeltsin promises to devote more resources to pensioners, farmers, and unpaid state workers left behind by reform.

In the new ruling troika, security chief Lebed and Chernomyrdin will be key in turning Yeltsin's "order and care" policy into reality. The 46-year-old Lebed, who helped save Yeltsin's campaign, has won broad powers over the police and intelligence services to battle corruption and crime (page 50). Yeltsin's trusty standby Chernomyrdin, who won kudos for slashing monthly inflation from 20% to 1.2% during his 3½-year tenure, will continue to call the economic shots.

The balance of power between the two is likely to keep shifting. If the former general makes even a little progress toward cleaning up government and curbing Russia's powerful *mafia*, he may well be Russia's next



PRIME MINISTER CHERNOMYRDIN (LEFT) AND SECURITY CHIEF LEBED WILL DUKE IT OUT IF PRESIDENT YELTSIN'S HEALTH SHOULD FAIL

President. Yeltsin seems to consider Lebed his heir apparent. But according to the Russian constitution, if the President becomes incapacitated, the Prime Minister takes over until a new election is held within three months. Chernomyrdin would become top dog if Yeltsin should die or become too ill to do the job.

Yet for all the competition between them, Lebed and Chernomyrdin could turn out to be an effective duo. They have timing on their side. After suffering through a four-year depression, the Russian economy is on the verge of recovery. Inflation has stabilized, and 80% of business is in private hands. Forecasts are predicting that growth, powered by raw-materials exports, construction, and services, will range from 3% to 6% a year between 1997 and



Russia's Agenda for "Order and Care"

SECURITY

Crack down on criminal gangs and corruption by boosting law enforcement, introducing witness protection, and forcing government officials to declare their income and assets. Turn the army into a professional military force.

ECONOMY

Keep inflation low and the budget deficit below 4% of GDP. Issue bonds on the European market to finance government debt and free domestic funds for industrial investment. Crack down on tax cheats.

SOCIAL ISSUES

Boost spending on health care and on services to the elderly. Privatize the pension system. Press employers to pay wages on time or face penalties.

FOREIGN POLICY

Push for all-European security system in a bid to discourage NATO expansion eastward. Downplay the notion of a "Russian threat." Break down trade, financial, and other barriers separating Russia, Ukraine, and Belarus.

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and traffic in illegal drugs and smuggled liquor. The weekend following the election, *mafia* leaders and many business people fled the capital as word circulated that Yeltsin had signed a decree to start a broad anticrime sweep.

Lebed will take immediate control of law-enforcement agencies that in the past have protected the extortionists they were supposed to punish. He is also drawing a bead on the criminals' high-level government patrons. Moscow's leading daily, *Izvestiya*, reported soon after the vote that Lebed was investigating former First Deputy Prime Minister Oleg N. Soskovets and two other ousted Yeltsin aides for their possible role in industrial-metals smuggling. Many believe Lebed is sending an early warning of how he plans to operate. A high-profile corruption case would rattle government officials and bureaucrats throughout the country, many of whom have amassed huge illegal fortunes over the past five years. Some used connections at production companies to obtain oil or metals at subsidized prices. They resold the commodities abroad at market prices and pocketed the difference. Others collected fat payoffs for steering government accounts to friends in the corrupt banking system.

Cracking down on tax evaders also has high priority on Lebed's agenda. In the first six months of this year alone, tax deadbeats cost the government \$15 billion in lost revenues. Under Lebed, businesses will be required to keep a single set of books and a single bank account, making it easier for the government to track incomes and profits. A team of investigators will be established to deal with the biggest cases. And the tax authorities will get a centralized computer system to aid in tracking down deadbeats.

If Lebed's anticrime campaign succeeds, his power will be formidable. But his ambitions extend well beyond police work. He wants to have influence over everything from economic issues to cultural affairs and foreign policy, and he has announced some highly nationalistic goals that smack of paranoia. In his first days in office, for example,

2000, compared with an estimated 1% to 2% this year. The Yeltsin team will spur the economy by cutting interest rates, reforming the tax system, and breaking up monopolies.

Thanks to such efforts, Yeltsin's reelection is likely to bring fresh capital flowing into Russia. Overseas investors have already begun to pour money into stocks, more than doubling total market capitalization since March. Direct investment will start coming in now that political uncertainty has been resolved. Just as important, the estimated \$40 billion that nervous Russians have socked away in Western banks could begin to trickle back. "The business community wasn't looking for Yeltsin to win as an individual," says Maxwell Asgari, president of ABB Russia. "What was important was whether his reform

system would continue. It's clear it will."

But the Yeltsin team still has huge problems to solve as it greases the wheels of growth. Crime is so rampant that many business people must hire bodyguards or learn self-defense. Property and shareholder rights are virtually ignored, discouraging investment. The tax system needs an overhaul to end chronic confusion and evasion. Businesses are subject to dozens of taxes that can add up to more than 50% of revenues. Enforcement is arbitrary.

CRIME SWEEP. Although Lebed and Chernomyrdin seem equally committed to bringing more order to Russia's free-for-all economy, the former paratrooper will lead the charge. His first target is Moscow's dozen criminal gangs, which shake down legitimate businesses, fix prices at food markets and taxi stands,

Yeltsin has promised to devote more resources to the pensioners, farmers, and others left behind by reform

he proposed banishing foreign religious groups and instituting other measures to combat Western cultural influence.

Such hard-line rhetoric helped sway voters. But it has also raised eyebrows at home and abroad. Comments such as "He who shoots first laughs last," made during a press conference the day before the election, do little to reassure people that Lebed cares about civil rights. And some Russians question his commitment to democracy and the free market now that the election is over.

It is probably overblown to depict Lebed as a shadowy militarist with dictatorial ambitions. "I'm no monster," he said at a recent press conference after the votes were counted. "I have no need for power just for the sake of exercising power." But with his sharp tongue and gruff demeanor, Lebed could fall on his face politically. Says Viktor A. Kremynenuk, deputy director of the government-sponsored USA-Canada Institute: "Lebed has disrupted the very delicate internal balance within the administration."

A key element of that balance, and a serious potential rival to Lebed, may prove to be Chernomyrdin. Just two days after the elections, he brusquely reasserted his control over economic policy. But the Prime Minister will have his hands full. He faces a crushing short-term budget crisis brought on by poor tax collection and some \$11 billion worth of spending promises during Yeltsin's campaign.

GOOD FAITH. The federal budget deficit has jumped to 7.5% of gross domestic product, up from 4.2% at the beginning of the year. If the government can't narrow the gap to 4% by the end of the year, it stands to lose a crucial \$10 billion loan from the International Monetary Fund. Chernomyrdin says he is ready to curb tax exemptions and take urgent measures to raise tax collection, imposing severe fines on overdue pay-

ments or even taking control of delinquent companies. The IMF is likely to be lenient if the government makes a good-faith effort to cut the deficit.

Falling interest rates will also help cut the government's borrowing costs. The annual yields on Treasury bills had zoomed to more than 200% in May, when buyers feared Yeltsin might lose. Following the election, the rates dropped to 77%.

WHAT GENERAL LEBED IS THINKING

Security chief Lebed wrote detailed answers to questions from BUSINESS WEEK about his plans. Here is a summary:



ON THE 'RUSSIAN THREAT'

We no longer follow the messianic communist idea, and we have no need to propagandize by using force. Russia has enormous natural resources and vast territories that as yet are barely being mastered and exploited. Therefore, we have no reason whatsoever to redraw the political map of the world.

Once we manage to establish a reasonable and dignified way of life in our own country, I think there'll be no end of countries that want to get on friendly terms with us.

ON NATO Of course, I am not enthusiastic about the extension of the NATO military bloc as it approaches Russian borders.... If we are "squeezed out" of Europe, then we shall be obliged to seek allies in the East.

ON CORRUPTION Government officials above a certain rank will be obliged to declare their total incomes and expenditures, along with those of all their family members and close relatives, each year or even every quarter. If they cannot prove that any property was legally acquired, then it will revert to the state.

ON CENTRAL PLANNING There will be no more loud, ideologically oriented reforming campaigns for total nationalization or mass privatization. Now we need consistent, steady, and reasonable work to reform the economy and society.

Lower T-bill rates should lead to a cut in commercial interest rates. That will give a much-needed boost to Russian enterprises, which were paying 100% to borrow. Across the country, enterprises have been hurting, especially in heavy industry. Up to now, Yeltsin has attacked inflation at the expense of industrial production, which is 50% of what it was four years ago. That could begin to change in 1997, as Russian banks and trading companies put some of their profits into industry.

While Lebed tackles corruption and

Chernomyrdin struggles with the budget, Yeltsin must move on to Reform Part II. That means restructuring sectors still untouched by privatization, such as defense and health care. Perhaps the biggest job will be introducing market economics to the agricultural sector, where the government still subsidizes unprofitable collective farms.

Yeltsin's first step, however, is likely to be more protectionist than market-driven. He seems ready to impose tariffs to protect Russian agriculture and newly privatized industry. In this, he is yielding to the voices of politicians who want Russia to follow the model of postwar Japan, letting its industries grow behind a protectionist wall.

While trying to build Russia's economic clout, Yeltsin also has social promises to keep. During his campaign, he pledged to raise pensions for the elderly and to pay back wages for millions of workers at cash-strapped state enterprises. On the drawing board are plans to build a private pension system and to beef up health care. But the budget crunch means Russia may have to grow for several years—and collect more taxes—before such promises are kept.

Nevertheless, Russians showed that they are determined to weather the economic pain of converting to capitalism. Yeltsin's victory, and the Lebed-Chernomyrdin agenda, effectively ensure that politi-

cians in the future will battle over how to manage the free market, not whether to abolish it. "A two-party system is developing in Russia," says Gennady Zyuganov, Yeltsin's challenger, who is trying to transform his campaign coalition of leftists and nationalists into an effective opposition party. In future presidential elections, which Russian are already beginning to take for granted, voters will decide between two candidates, not two systems.

By Patricia Kranz, with Rose Brady, in Moscow

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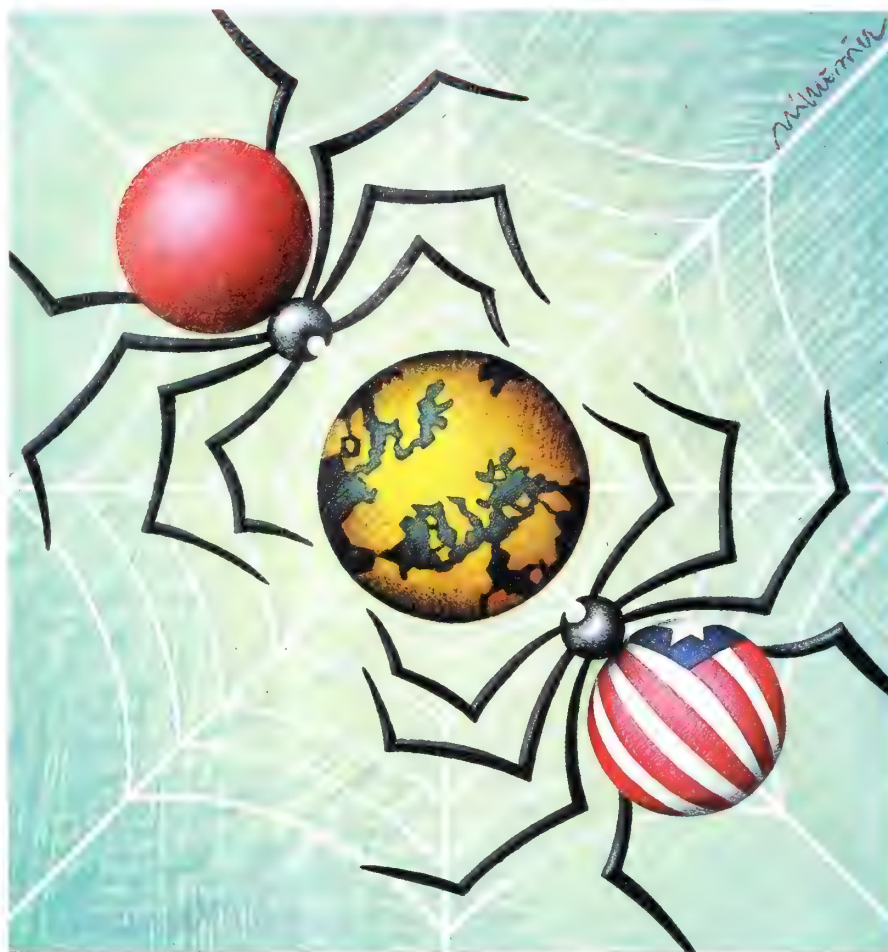
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JAPAN

KEIRETSU CONNECTIONS

The bonds between the U.S. and Japan's industry groups

Amid rolling hills outside Nagoya, Toshiba Corp. recently took the wraps off a new \$1 billion chip-making facility that uses ultraviolet lithography to etch circuits less than one micron wide—a tiny fraction of the width of a human hair. Toshiba aims eventually to turn out next-generation, 64-megabit chips with 70% fewer parts and 40% more efficiency.

A decade ago, such advances would have inspired fear in IBM's boardroom. Not this time. The Toshiba chip site owes much to a strategic alliance with IBM and Siemens of Germany. In fact, IBM's

knowhow in chemical mechanical polishing, essential to smoothing the tiny surfaces of multilayered chips, played a critical role. "We had little expertise here," concedes Toshiba's Koichi Suzuki.

QUIET CHANGE. What's more, about 20 IBM engineers will show up shortly to transfer the technology back to an IBM-Toshiba facility in Manassas, Va. In addition to the semiconductor cooperation, IBM and Toshiba jointly make liquid-crystal display panels—even though they use the LCDs in their fiercely competitive lines of laptop computers. "It's no longer considered a loss of corporate manhood to

U.S.-JAPANESE WEBS

TOSHIBA-IBM Sharing the \$1 billion cost of developing a 64mb and 256mb memory chip facility, technology that will be transferred to a new IBM plant in Virginia.

MITSUI-GE GE's power-systems unit has picked up Asian contracts with Mitsui's well-connected bank. GE has the technology; Mitsui has the contacts and deep pockets.

TOYOTA-GM, TRW GM's parts division, Delphi, supplies components to Toyota. Participates in Toyota's *keiretsu* strategy meetings. Similarly, TRW says it has become part of the Toyota group.

CANON-HP The two share laser-printer technology, and Hewlett-Packard buys engines from Canon, but the two still compete with end products around the world.

MITSUBISHI-CATERPILLAR A long-time joint venture has emerged as Cat's primary Asian manufacturing source. American and Japanese staff jointly designed a successful excavator line made in Japan, the U.S., Indonesia, and China.

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let others help out," says IBM Asia Pacific President Robert C. Timpson.

What's going on? Call it alliance capitalism. For years, many U.S. tie-ups with Japanese companies tended to be defensive in nature, poorly managed, and far removed from core businesses. Now, the alliances are deepening, taking on increasingly important products, and expanding their geographic reach in terms of sales (table). U.S.-Japanese partnerships are, for example, popping up in Asia's emerging but tricky markets, reducing the risks each company faces.

This deepening web of relationships reflects a quiet change in thinking by Japanese and U.S. multinationals in an era when keeping pace with technological change and competing globally have stretched the resources of even the richest companies. "The scale and technology are so great that neither can do it alone," says Jordan D. Lewis, author of *The Connected Corporation*.

Overall, instances of joint investment in research, products, and distribution by Japanese companies and foreign counterparts, mostly American, have jumped 26%, to 155, in the first quarter of 1996—on top of a 33% increase between 1993

SOLUTION

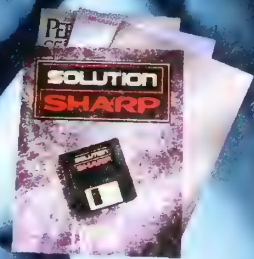
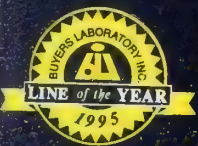
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1994 Study

and 1995—according to the Sakura Institute of Research.

The growing links complicate the perennial debate about U.S. trade deficits with Japan. Official trade statistics track only the small universe of U.S. products made in America and shipped to Japan. They don't capture the value of American-branded products made in Japan as part of an alliance. These tie-ups also blur the difference between corporate and national interests. True, Eastman Kodak Co. has marshaled the Clinton Administration to back its bid to crack Japan's allegedly rigged market. Yet how many Americans realize that Kodak and archrival Fuji Photo Film Co. have for years collaborated in joint research on a new advanced photo system?

ENVY. And while Uncle Sam and U.S. companies with grievances have attacked Japan's system of big industrial groups, called *keiretsu*, as exclusionary, other chieftains of Corporate America have quietly become stakeholders of sorts. The list includes companies as diverse as IBM, General Motors, TRW, Boeing, and Caterpillar. All of this "represents a very significant constraint on what the U.S. gov-

come a second-tier member of the Toyota and Nissan groups. That means TRW has long-term supplier ties, but neither Japanese company actually owns equity in TRW. "Both Toyota and Nissan are among the top 10 customers of TRW worldwide," says Gorman.

GM's sprawling parts division, Delphi Automotive Systems, also has become

"It's no longer considered a loss of corporate manhood to let others help out"

an insider of sorts. Last year, it sold \$400 million in parts to Toyota Motor Corp. and other Japanese companies—and expects to double that figure in five years. In fact, Delphi is now the Japanese auto maker's No. 1 foreign supplier. It participates in Toyota's quarterly *kyoho-kai*, or *keiretsu*-member strategy sessions.

Nobody is suggesting that U.S.-Japan

ground in their level of cooperation. The impact is felt far beyond the U.S. and Japanese home markets. Take the 50-50 venture between Caterpillar Inc. and Mitsubishi Heavy Industries Ltd., part of Japan's \$200 billion *keiretsu* of the same name. Early on, Cat wanted a way to sell its construction equipment in Japan and compete with rival Komatsu Ltd. on its home turf. Mitsubishi wanted to play catch-up with Komatsu, too, and expand its export markets.

Their alliance played a key role in taming Komatsu. But the partners have broader ambitions. Since Cat shifted all design work for its "300" series of excavators to the partnership back in 1987, the venture's two Japanese factories have emerged as Cat's primary source of production for sales to fast-growing Asia. The alliance's products reach the world market through Cat's network of 186 independent dealers in 197 countries.

EURO-ANGST. Even General Electric Co., which has done well on its own in Japan, found it useful to tap Japan's trading houses and banks for big-ticket project financing in Asia. Earlier this year, GE and Japanese trading company Mitsui Bank Ltd. picked up an \$85 million contract in China for two steam turbines, with Mitsui the lead contractor. The two also have teamed up on an Indonesian power project. Why join forces with Mitsui? "They're an important source of financing," says Orit Frenkel, GE's senior manager for international trade.

Some Europeans are beginning to voice concern that the deepening pattern of alliances may hurt their interests. While it's true that both U.S. and Japanese companies have links with European partners, the number of U.S.-Japanese tie-ups is growing faster. "The largest, most sophisticated economies in the world are getting together, and they are getting most of the benefits of this," says Ulrike Schaeede, a German who is assistant professor of economics at the University of California at San Diego.

So the partnerships are not only reshaping the contours of U.S.-Japanese rivalry in fascinating ways; they're also having surprising ripple effects around the world. As they evolve into even more complex webs centering on technology or new markets, the trend "is beginning to push the traditional boundaries of what competition means," says Walter E. Shill, a principal at McKinsey & Co. in Tokyo. Sorting out the winners from the losers will forever be more difficult.

By Brian Bremner in Tokyo, with Zachary Schiller in Cleveland, Tim Smart in Fairfield, William J. Holstein in New York, and bureau reports



ATTACK CAT: A tie-up with Mitsubishi lets Caterpillar manufacture in Asia

ernment can do without hurting its own players," says Yale University professor Mark Mason, author of *American Multinationals and Japan*.

Many American executives who have established these alliances say they appreciate the attributes of Japan's big industrial groups. U.S. managers have always envied the *keiretsu* edge in spreading risk over a cluster of companies when betting big on a new technology or blitzing emerging markets. TRW Chairman Joseph T. Gorman, for example, is proud that his company has be-

come economic rivalry has suddenly vanished. Far from it. Toyota may be peddling GM's Cavalier under its own brand name through dealerships in Japan. But that hasn't stopped GM from setting up a joint venture in Thailand to challenge Toyota's dominance or from planning to bring a right-hand-drive version of its Saturn sedan to Japan in 1997. While Hewlett-Packard Co. and Canon Inc. share laser technology for printer engines, they still bang heads for sales worldwide.

Yet in one industry after another, U.S. and Japanese partners are breaking new

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EDITED BY SHERI PRASSO

SUHARTO'S GRIP IS LOOSENING: WHO WILL COME NEXT?

After President Suharto's wife of 49 years died in late April, a frequent visitor to the 75-year-old leader remarked: "His face looks so sad—older, weaker, and lonely." So when Suharto flew to Germany in early July to undergo medical tests, few observers were surprised. Although doctors gave him a clean bill of health for a man his age, he's believed to suffer from a heart condition complicated by diabetes, kidney stones, and prostate ailments.

Thus, it could be the beginning of the endgame for one of Asia's last authoritarian patriarchs. For the 31 years Suharto has ruled Indonesia, the opposition and the press have been firmly muzzled, elections safely rigged, and the military brass reshuffled without incident. As long as Suharto could keep the economy growing 8% a year, he could delay picking a successor.

Today, many analysts believe Suharto lacks the stamina to run this nation of 190 million people much longer, particularly now that a credible political opposition has emerged. Several possibilities of how power might be shared in the near future are being bandied about, most of which give Suharto a backstage role. In one scenario, the presidency would go to a loyal army general, either Vice-President Try Sutrisno or Special Forces Commander Prabowo Soemito Subianto, his son-in-law.

NEW TARGET. Diplomats say a recent split in the armed forces would not leave any of Suharto's six grown children with enough support to inherit all of his political power. That could leave their deals with foreign multinationals at risk. Duty-free privileges for South Korean auto maker Kia Motors Corp., linked up with Suharto's son Tommy, could be withdrawn if the opposition takes power. Another target could be Suharto's son Bambang Trihatmodjo's PT Bimantara Citra, which has joint ventures with Hyundai, Ford, Union Carbide, NEC, Sumitomo, Kawasaki, Nestlé, and others.



SUHARTO: *Losing stamina?*

The prospect of troubles for the Suhartos must please opposition leader Megawati Sukarnoputri, daughter of Suharto's deposed predecessor, President Sukarno. Sympathy for her once powerless Indonesian Democratic Party surged after the government orchestrated her ouster from the party chairmanship in June.

A messy succession is the last thing Indonesians want. Anyone older than 35 remembers the hundreds of thousands of innocent people, mainly ethnic Chinese, who were slaughtered in the streets in 1965 when Sukarno was deposed in a failed communist coup. That horror gave then Major General Suharto justification to repress dissent for three decades.

But economic prosperity has created higher political expectations, and repression may not work much longer. The key signal came in June, when the sacking of Megawati from her party provoked the unthinkable—clashes between thousands of middle-class Indonesians and riot police in the streets of Jakarta.

Just as Suharto has backslid on promises of political openness, economists fear he may fail to deliver on promises to remove barriers to trade and investment. Instead, he has been protecting his children's ubiquitous business interests. "As long as the father is there, they will get privileges," says Christanto Wibisono, director of Indonesia Business Data Center.

"But the moment he has no more power, we will see the restructuring of economic forces."

Such talk knocked 4% off of the Jakarta Stock Exchange before the market showed signs of recovery on July 9. The two listed holding companies of Suharto children were among the hardest hit. To safeguard his offspring's wealth, Suharto must soon confront the issue of a controlled succession—before political turbulence leaves him with no choices to make.

By Michael Shari in Jakarta

GLOBAL WRAPUP

DEUTSCHE BANK'S NEW LOOK

► Frankfurt's Deutsche Bank is reorganizing to better compete in the big leagues of global finance. Chairman Hilmar Kopper on July 9 divided Europe's largest lender into four divisions: private banking, commercial and institutional banking, investment banking, and a unit handling information technology and other internal functions.

The reshuffle will help to cut costs and simplify Deutsche's complex management structure. Deutsche's

announcement follows similar moves by Credit Suisse and Swiss Bank Corp. But the model for the makeover is Deutsche Morgan Grenfell, Kopper's London-based investment banking unit, where managers already have global responsibilities and clear reporting lines.

CAN AIRBUS PARTNERS UNITE?

► After years of British prodding, Europe's Airbus Industrie partners have agreed to convert the consortium from a loose joint venture into

an independent company by 1999. Today, Airbus' French, German, Spanish, and British industrial partners manage by committee and build plane components with little competitive bidding. With Airbus losing market share to Boeing Co., the intention is to cut costs and better manage new projects.

But agreeing about which industrial assets should be put in the new company will be difficult. The biggest sticking point is France's Aérospatiale, which is reluctant to give up its design unit that now oversees Airbus programs.



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COMING, A VACCINE THAT CAN LICK LYME DISEASE?

VACCINES FREQUENTLY USE A protein isolated from bacteria to jolt the immune system—which creates defensive cells with long memories. The next time the body is invaded by a microbe that displays the same protein, the immune cells remember it and spring to alert, releasing antibodies that attack the invader. But some bacteria that inhabit multiple hosts—the microbe that causes Lyme disease is one—change the proteins on their outer surface when they migrate from, say, an insect to a mammal host. If you are vaccinated with proteins isolated from Lyme bacteria in a tick, your immune system may not recognize the mi-

crobe in your bloodstream.

In the case of Lyme disease, researchers at MedImmune Inc. in Gaithersburg, Md., think they have a solution to the problem. It's a protein called DBP that seems



DEER TICK: *Hosting protean proteins*

to be present on the Lyme bacterium for at least four days after it enters an animal or human host—enough time for the immune cells to start producing antibodies.

That could be an advantage over the other leading candidate for a Lyme vaccine, a protein called Osp A that is present on Lyme bacteria in ticks, but apparently not in humans. To acquire enough antibodies to kill the bacteria as soon as the tick bites—before the bacteria's surface protein changes—people in infested areas would probably need boosters at the start of each tick season. Even so, it would be a major advance. SmithKline

Beecham PLC is now conducting human trials with Osp A and should know by late November if it works. Human trials for MedImmune's DBP are still months away. □

THIS SHOCKER IS GOOD NEWS

DOCTORS YELLING "CLEAR!" and applying electrified paddles to stopped hearts are all-too-familiar scenes on emergency-room TV dramas. But the reality is that nearly 1,000 Americans die suddenly each day from cardiac arrest—chaotic electrical rhythms that stop the heart's pumping action—because they don't get that vital shock in time. Defibrillators must be used within minutes of cardiac arrest. Yet they have typically been heavy, expensive devices that are hard to transport and maintain.

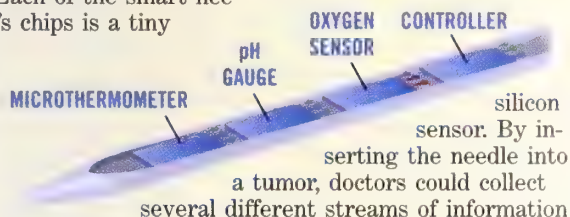
By early fall, however, that could change. The Food & Drug Administration is expected to approve a portable defibrillator called Forerunner, made by Seattle's Heartstream Inc. It's a compact plastic-encased device about the size of a hard-bound book, weighing just four pounds. At \$3,000 to \$4,000, it will cost less than half as much as some rival instruments. People with no medical background can learn how to use Forerunner in minutes, thanks to a combination of a user-friendly design and sensor pads that determine whether defibrillation is necessary or not, says Heartstream CEO Alan Levy. Getting more emergency vehicles to carry the new defibrillators is Levy's first goal. But he also hopes the machines someday will become common life-saving equipment in sports arenas, on airplanes, and in other public locations.

Joan O'C. Hamilton

A NEEDLE WITH SUPERSHARP SENSORS

THIS SUPERTHIN NEEDLE'S SMARTS ARE IN THE GROOVE. Embedded into a slot near its point is a thread-size strip of computer chips. The chips don't make it easier to sew on a button—they're designed to help diagnose and track the course of human illnesses.

Each of the smart needle's chips is a tiny



about the cancer, such as its growth rate or its likely response to chemotherapy. Similar probes in use today are 30% fatter—and doctors often must insert more than one, since they carry only single-purpose sensors. The smart needle, which is also cheaper to manufacture than other probes, can take measurements with up to eight different sensors, says researcher Kenneth S. Szajda of the Health Sciences & Technology joint program between Harvard University and Massachusetts Institute of Technology. One sensor is a microthermometer for highly localized temperature readings. Szajda is now designing chips for measuring oxygen concentration and acidity in the body. Like the microthermometer, the new chips will also digitize signals so they can later be read by computer.

Otis Port

INNOVATIONS

■ Ships plowing through the ocean create wakes that can stretch for miles. Satellites use these trails to locate ships, and torpedoes are designed to follow them. The Navy wants to reduce wakes from its next-generation warships—and the latest crop of high-power computers may make that possible. Researchers at Rensselaer Polytechnic Institute are creating a software model to study the mechanics of wake formation.

■ Japan's Rocket System Corp. (RSC) may become the newest rival in the commercial space-launch business. It is negotiating with Hughes Electronics' Space & Communications unit, which wants to buy a block of satellite launches starting around 2000. RSC will use the Japanese space agency's H2A rocket, which will put a satellite into orbit for about \$75 million—a price Hughes calls "competitive" with other launch services.

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwjul@businessweek.com

TELEVISION

HUGE, CLUNKY—AND MAYBE THE FUTURE

An east German laser TV system has the world watching

It sounds like just the kind of television you would expect from the former East Germany: It weighs 220 pounds, sucks up 10,000 watts of electricity, and requires a refrigerator-size cooler to keep it from melting down.

A German television that draws pictures with laser beams doesn't seem the sort of thing managers at Thomson, Sony, or Philips Electronics should lose sleep over. And yet TV makers everywhere are keeping an eye on the progress of Christhard Deter, the engineer behind a 25-employee company called Laser-Display-Technologie (LDT) in the industrial town of Gera. "Deter's ideas are world-class," says Glenn H. Sherman, CEO of Laser Power Corp., a San Diego maker of laser gear.

The curiosity about LDT is understandable. Engineers have bandied about ideas for laser TV sets since the 1970s. Advances in optical technology mean they could go mainstream in the early 21st century. And Deter's prototype, though still primitive, creates images that are bright, colorful, and razor-sharp. **GHOSTBUSTERS.** The pictures can be projected onto a surface measuring up to 10 feet diagonally. Alternatively, the whole mechanism can be built into a rear-projection box that resembles a conventional wide-screen TV. The prototypes will handle any program format. LDT holds 10 patents on the technology and is poised to unveil a more sophisticated prototype for professional markets such as theaters and conference halls in November.

How did this upstart carve out a niche in a field dominated by giant Asian and European competitors? Deep-pocketed German backers, for one thing. Together, Schneider Rundfunkwerke—a German TV maker—and a Daimler Benz subsidiary called Temic Telefunken Mi-

THE COMPETITION IN PROJECTION TELEVISION

PROJECTION CRTs An assembly of three bright CRTs creates images from 30 inches (diagonal) up to 15 feet (Thomson, Hitachi, Toshiba, and others)

PROJECTION LCDs LCD systems require a powerful light source and complex optics but take up less space than CRT projectors (Sharp, Sony)

DIGITAL LIGHT PROCESSING TI's technology can create 25-foot images from light reflecting off of thousands of tiny mirrors etched on silicon (In Focus Systems, Proxima, nView)

HUGHES-IVC LIGHTVALVE A high-resolution CRT draws an image on a light amplifier, which creates 50-foot pictures

croelectronic have committed about \$100 million to realizing Deter's vision. Schneider hopes lasers will revive its founding TV business. Daimler plans to sell lasers and other components to Schneider and other companies that license the technology. Throw in the cooperation of optics giant Carl Zeiss Jena, and Deter's laser effort is nothing less than a national effort by Germany to regain a position in consumer electronics.

The backers have their work cut out for them. LDT must squeeze out cost and bulk, perfecting components that can be mass-produced cheaply. "It will take an enormous effort to get to a [commercial-

ly viable] television," concedes LDT Vice-President Klaus Bomhardt.

Even as a prototype, however, the machine is a marvel. Instead of shooting electrons at a phosphorescent screen, like cathode-ray tubes in most TVs today, Deter's design manipulates a single beam of ever-changing color. Deflected by two mirrored scanners and passed through a lens, the light sweeps across 1,152 horizontal lines at 56 miles per second. At a recent demonstration, life-size dancers gyrated on the screen in crisp definition, and without the annoying ghost images of a conventional TV caused by the afterglow of phosphors.

Conference planners could use laser TV projectors to produce bigger, brighter displays of video, data, and computer-generated images. Advertisers could use them to promote products at football



CHRISTHARD DETER: *How soon a home model?*

games and rock concerts. Eventually, however, the biggest market for big-screen TV will be the home. And to attract individual buyers, Deter will have to compete head-on with projection TVs that now retail for as little as \$900.

That's why Deter wants to ditch the clunky and expensive gas lasers. With the help of several U.S. companies and some German universities, he hopes to switch to cheap, small semiconductor lasers. The hitch: The diminutive components—also called laser diodes—pro-



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HOLLYWOOD

PLENTY OF DREAMS, NOT ENOUGH WORKS?

But a flurry of new projects could yield a hit

duce only red and green light, not blue. And they don't generate enough light to create a bright TV image. Sony, IBM, Philips, and others are trying to develop true-blue laser diodes. But those are several years from commercialization.

So Deter and his colleagues have hit on an interim solution: They're using an ordinary solid-state infrared laser and amplifying it with laser diodes. Then they chop the light stream into pulses. Next, they channel the pulses through tiny crystals that alter the wavelength to create streams of red, green, and blue light that can be combined to produce every color in the rainbow. In lab tests, this approach has cut energy usage 80%.

The next big cost savings—and Deter's most celebrated innovation—is in electromechanics. To create a picture line by line, the laser TV uses an ingenious assembly of mirrors to control vertical and horizontal scanning. The mechanism remains a little clumsy and difficult to assemble. So Deter is replacing it with fingernail-size silicon wafers coated with silver that flick up and down in response to an electrical pulse. In mass production, the simpler of the two mirrors could cost as little as \$13 apiece, Deter figures, vs. \$3,300 now. A production version could be ready in as little as two years.

SMART IDEAS. There's no time to lose. U.S. consumers alone will purchase nearly a million projection-TV sets this year that use cathode ray and liquid-crystal-display technology. Five companies have announced products based on Texas Instruments Inc.'s "digital light processing" (table, page 60). And Japanese companies have demonstrated large, flat-panel screens using gas-like plasma.

These displays are cheaper than Deter's laser system and are available now or will be soon. Projection TVs with 60-inch screens run about \$2,800. Digital light processing devices for conference halls and theaters range as high as \$12,000. Deter's models, in contrast, will cost around \$65,000 at launch—as much as giant, custom-made displays used in stadiums. Bomhardt says the price should drop to \$2,000 in several years. But rival systems are also getting cheaper. "The industry is moving rapidly," says consultant Frederic Kahn in Palo Alto, Calif.

On the other hand, other companies, Sony Corp. included, see enough potential in laser TV to keep research efforts going. If laser does prevail in the next century, Deter has a head start in mechanical components. He also has plenty of smart ideas, and the financial backing to realize them. What a switch from the days of the Iron Curtain, when only the ideas were in real abundance.

By David Woodruff in Gera, Germany, with Neil Gross in New York

There's nothing Hollywood loves more than a good show. And in late May, DreamWorks SKG—the new studio being hatched by entertainment superstars Steven Spielberg, Jeffrey Katzenberg, and David Geffen—put one on.

Commandeering space on the Universal back lot, the Dream Team lit up a soundstage with coming attractions: clips of George Clooney and Nicole Kidman on location in Manhattan shooting DreamWorks' first movie, *The Peacemaker*, and then an ear-shattering rock video by singer George Michael. Lyricist Stephen Schwartz crooned songs from *The Prince of Egypt*, an animated film scheduled for a 1998 release. Playing to a select audience of 150 employees, investors, bankers, and joint-venture partners, Katzenberg announced: "This is show-and-tell time."

Indeed. Twenty-two months after DreamWorks was launched with great fanfare, what do the three moguls have to show for themselves? Precious little that the general public can see, hear, or play. The studio produced two television shows last season, with dispiriting results: *Champs* was quickly canceled, and *High Incident* barely got picked up for next season. The film unit has gotten off to a slow start because Spielberg, who heads it, has been busy fulfilling commitments to make several films for other studios. *The Peacemaker*, directed by *E.R.* director Mimi Leder, won't be out for about a year, and Spielberg's first directorial effort for the studio likely won't get inside a cineplex until mid-1998.

What's more, the studio is six months ahead of schedule in its expenditures. With 800 employees and substantial cap-

ital outlays to build a new studio, fund joint ventures in interactive games and video arcades, and launch a consumer-products division. DreamWorks is spending its \$2.7 billion in capital at a clip of \$400 million a year. Profits are five years away at best. Factor in Hollywood's treacherous economic climate—a glut of product, skyrocketing expenses, and studios' reliance on big film libraries in lean times—and any new studio's long-term viability looks tenuous.

WHAT'S TO WORRY?

With their star quality, Katzenberg, Spielberg, and Geffen can strike desirable deals with the likes of Sega and ABC



But this is Hollywood, and no one is worried. DreamWorks' bankers, investors, and joint-venture partners are uniformly enthusiastic about the studio's progress. Even other showbiz executives say DreamWorks will make it. The law of averages, they figure, favors proven hitmakers like Spielberg, Katzenberg, and Geffen. "If anyone has a chance to make it, it's these three," says former MCA Inc. Chairman Thomas P. Pollock.

Clearly, DreamWorks' biggest asset remains the track records and reputations of its founders. Each is contractually bound to work exclusively for the studio for a decade, though Spielberg is allowed three extracurricular projects. But the Dream Team has a lot more than money and contracts fueling their drive to make DreamWorks work. Failing would be personally and professionally devas-

tating for the trio. "You're always competing with your own past," says Spielberg. "It's the reach muscle. You have to reach for something new in life. And with these guys, I have the Schwarzenegger of reach muscles." Adds Geffen, who acts as the group's chief dealmaker: "This is a marathon, not a sprint. Watch where we are at the end of the race. I would rather die than fail."

And despite its slow start, DreamWorks recently has been making deals and starting new projects at a fast clip. It just bought the music rights to the hit Broadway show *Rent*. It has two high-profile TV shows debuting this fall—ABC's *Spin City*, with Michael J. Fox, and CBS's *Ink*, with Ted Danson. In TV, DreamWorks is already "a major player," says CBS Entertainment President Leslie Moonves. "It's their ability to get the best talent in the business to come work for them."

To be sure, a good deal of top talent has flocked to DreamWorks. TV producers such as Gary David Goldberg and Linda Bloodworth-Thomason and filmmakers such as *Rain Man* producer Mark Johnson and *Crying Game* director Neil Jordan have all

signed on. To run its music unit, DreamWorks outbid Walt Disney Co. and others to land former Warner Music CEO Mo Ostin. Maury Povich and Connie Chung will do an interview show in 1998. Some of the hires—however well-known themselves—seem awed by their new bosses. "You can get some pointers from Steven Spielberg at one end of the company, then from Katzenberg at the other," marvels Danson.

60-YEAR STREAK. Leveraging their cachet as partners has enabled the Dream Team to negotiate some extraordinarily favorable deals. This is the new studio's secret weapon, and it may be what allows it to break Hollywood's 60-year streak of failed studio startups. Consider the deal DreamWorks struck to build a new studio in Playa Vista, a gritty suburb near the Los Angeles airport. The 1,087-acre parcel had been a white elephant for the developer, Maguire Thomas Partners, which for two years had been unable to attract a major tenant. So Maguire Thomas hired Jeffrey S. Berg, chairman of the ICM talent agency, to help. Within hours of the announcement that DreamWorks was being formed, Berg had Spielberg, Geffen, and Katzenberg trudging through the dusty site.

DreamWorks got quite a bargain. Maguire Thomas will raise \$7 billion to build DreamWorks a 100-acre studio complex, as well as other commercial and residential space. Lured by DreamWorks' presence, other entertainment tenants, including special-effects house Digital Domain and Silicon Graphics Inc., have signed on. The project also includes 13,000 homes. The developer is betting that true Angelenos would love nothing better than to live next door to a movie studio. DreamWorks even gets one-third of the cash generated as those homes are sold. For DreamWorks, the price of admission is only \$66 million, rather than the \$200 million it would have cost to build the studio on its own.

Indeed, DreamWorks is adept at persuading others to split



DREAMWORKS' DEEP POCKETS

Who owns and controls DreamWorks?

STAKE	PLAYER	INVESTMENT
22.2%	STEVEN SPIELBERG	\$33.3 MILLION
22.2%	DAVID GEFFEN	\$33.3 MILLION
22.2%	JEFFREY KATZENBERG	\$33.3 MILLION
18.5%	PAUL ALLEN	\$492 MILLION
11.2%	THE LEE FAMILY	\$300 MILLION
1%	MICROSOFT	\$27 MILLION
1%	CHASE CAPITAL PARTNERS	\$27 MILLION
1%	SEAGRAM	\$27 MILLION
1%	DIRK ZIFF	\$27 MILLION

DATA: BUSINESS WEEK

the bill for many of its ventures. On top of the \$27 million it invested for a 1% stake, Microsoft Corp. is sharing the \$30 million cost of DreamWorks Interactive, whose interactive-game products will be in stores this Christmas. "This [is] a very, very smart deal," says Microsoft Chairman William H. Gates III.

DreamWorks was also able to strike a remarkably sweet deal with ABC. Typically, the producer of even a hit show loses money on it until reruns can be sold in syndication after three seasons. ABC is picking up half of DreamWorks' tab for producing shows—even ones that don't air on ABC. If its shows make it to a second season on ABC, DreamWorks pockets half of the revenue ABC gets for ads during the show. "A lot of folks see that as a very one-sided deal," says former HBO Chairman Michael J. Fuchs. Retorts ABC network chief David Westin: "We didn't give away the store. We're in business with guys who know what it means to make hits."

DreamWorks has also formed a partnership with Sega Enterprises Ltd. to launch a chain of 30,000-square-foot video-game arcades. By the end of the decade, DreamWorks and Sega plan to have 100 to 125 in malls and downtowns across the country. Spielberg, a game fanatic who will help design the arcades, personally helped pitch them to Melvin Simon, a shopping-mall titan from Indianapolis. That sort of megawatt assist is one reason Sega gave DreamWorks a 25% stake in the \$150 million venture for only \$10 million.

"THE MOTHER LODE." But in the high-risk, high-reward areas of film production and animation, DreamWorks prefers to go it largely alone. It will handle its own distribution in the U.S., thereby getting all the upside from any animation hit or Spielberg extravaganza but also paying most of the huge production and marketing costs. At the industry average of \$54 million per film, that adds up to big bucks, though the studio intends to release only 10 films a year. Major studios typically release 20 or more.

Even so, DreamWorks seems undaunted by the amount of money flying out of its coffers. Spielberg recently paid

a record \$2 million after just hearing a pitch about an autistic couple from *Rain Man* writer Ronald Bass. And Bass gets an additional \$1 million to write the script. "It was the most emotional pitch I have every heard," Spielberg told Katzenberg later. A little chancy, perhaps? DreamWorks regards any Spielberg project as being a sure thing. "I don't see this as a risk," says Katzen-

berg. "Can you think of a theater in this country [not taking] a Spielberg film?"

These days, Katzenberg spends three hours a day overseeing the animation unit, which expects to turn out a film a year starting in 1998. Animation, Katzenberg believes, is "the mother lode." *The Lion King* and *Beauty and the Beast* each brought in more than \$1 billion in tickets, video, music, and consumer products for Disney. And Katzenberg has done his best to re-create the Disney animation factory by hiring away from Disney 40 animators and key music writers Hans Zimmer, Schwartz, and Elton John.

But DreamWorks' plunge into animation is perhaps its riskiest endeavor. Other studios, and Spielberg himself,

have failed in the past to challenge Disney's supremacy. Disney's well-oiled publicity machine, including its ABC network and theme parks, will give its forthcoming *Bugs* a big send-off when it likely opens against *The Prince of Egypt*. Even though Katzenberg plans to build up his own promotional arsenal, "Disney isn't going to let these guys come in without a major fight," says Schroder Wertheim & Co.'s David Londoner.

All this activity, obviously, is incredibly expensive. DreamWorks will spend more than \$1.3 billion by 1998 before it even has a significant collection of revenue-generating products. But DreamWorks is building assets, and its investors are a patient lot. Microsoft co-founder Paul G. Allen committed \$492 million for an 18.5% stake, and Samsung Electronics heiress Mie Kyung "Miky" Lee put in \$300 million. Chase Manhattan Bank arranged a \$1 billion credit line. "I have a lot of money. I can wait," says Allen, who sees potential ways to fit his other media and technology ventures with DreamWorks' creativity.

SELL-OFF? How will everyone get their money out of DreamWorks? Down the road, a public offering is probable. A sale to a larger company is always an option. One possible acquirer could be MCA, which already distributes DreamWorks' music and videos in the U.S., as well as its movies in some international markets. "We haven't discussed anything like that, but I definitely want to stay in business with them," says Edgar Bronfman Jr., president of MCA parent Seagram Co.

But before any IPO and before any sell-off to a bigger entertainment empire, the DreamWorks trio will first have to start producing hit movies, TV shows, and music. Yes, much about DreamWorks is now real—the deals, the product pipeline, and the plans for the new studio complex. But the only reality that will count a few years from now is whether these well-pedigreed partners can deliver on the high expectations that swim around DreamWorks. Watching the trio pull it off will be the kind of show Hollywood really loves.

By Ronald Grover
in Universal City, Calif.

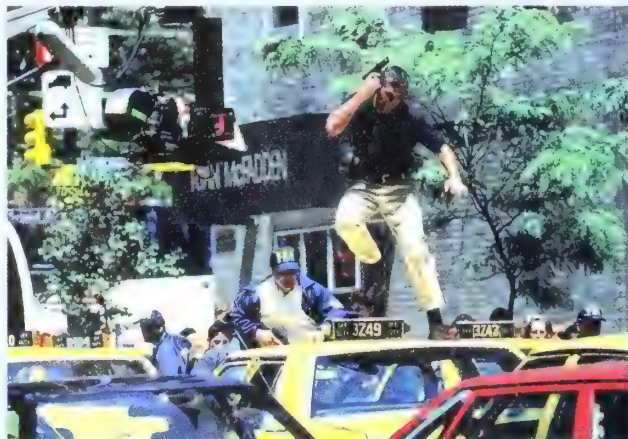
WHERE THE MILLIONS ARE GOING

By 1998, DreamWorks expects to run through at least \$1.3 billion of its investors' money, making it the costliest startup in entertainment history. Here's the breakdown

FILM STUDIO	\$800 MILLION
ANIMATION STUDIO	\$200 MILLION
TV PRODUCTION AND SYNDICATION	\$125 MILLION*
RECORD LABEL	\$20 MILLION
VIDEO ARCADES	\$10 MILLION*
INTERACTIVE COMPUTER GAMES	\$15 MILLION*
DIGITAL PRODUCTION FACILITIES	\$25 MILLION
EQUITY IN REAL ESTATE FOR NEW STUDIO	\$66 MILLION*

* Additional amounts paid by partners in venture

DATA: BUSINESS WEEK ESTIMATES



SHOOTING THE PEACEMAKER: DreamWorks' first flick

berg. "Can you think of a theater in this country [not taking] a Spielberg film?"

These days, Katzenberg spends three hours a day overseeing the animation unit, which expects to turn out a film a year starting in 1998. Animation, Katzenberg believes, is "the mother lode." *The Lion King* and *Beauty and the Beast* each brought in more than \$1 billion in tickets, video, music, and consumer products for Disney. And Katzenberg has done his best to re-create the Disney animation factory by hiring away from Disney 40 animators and key music writers Hans Zimmer, Schwartz, and Elton John.

But DreamWorks' plunge into animation is perhaps its riskiest endeavor. Other studios, and Spielberg himself,



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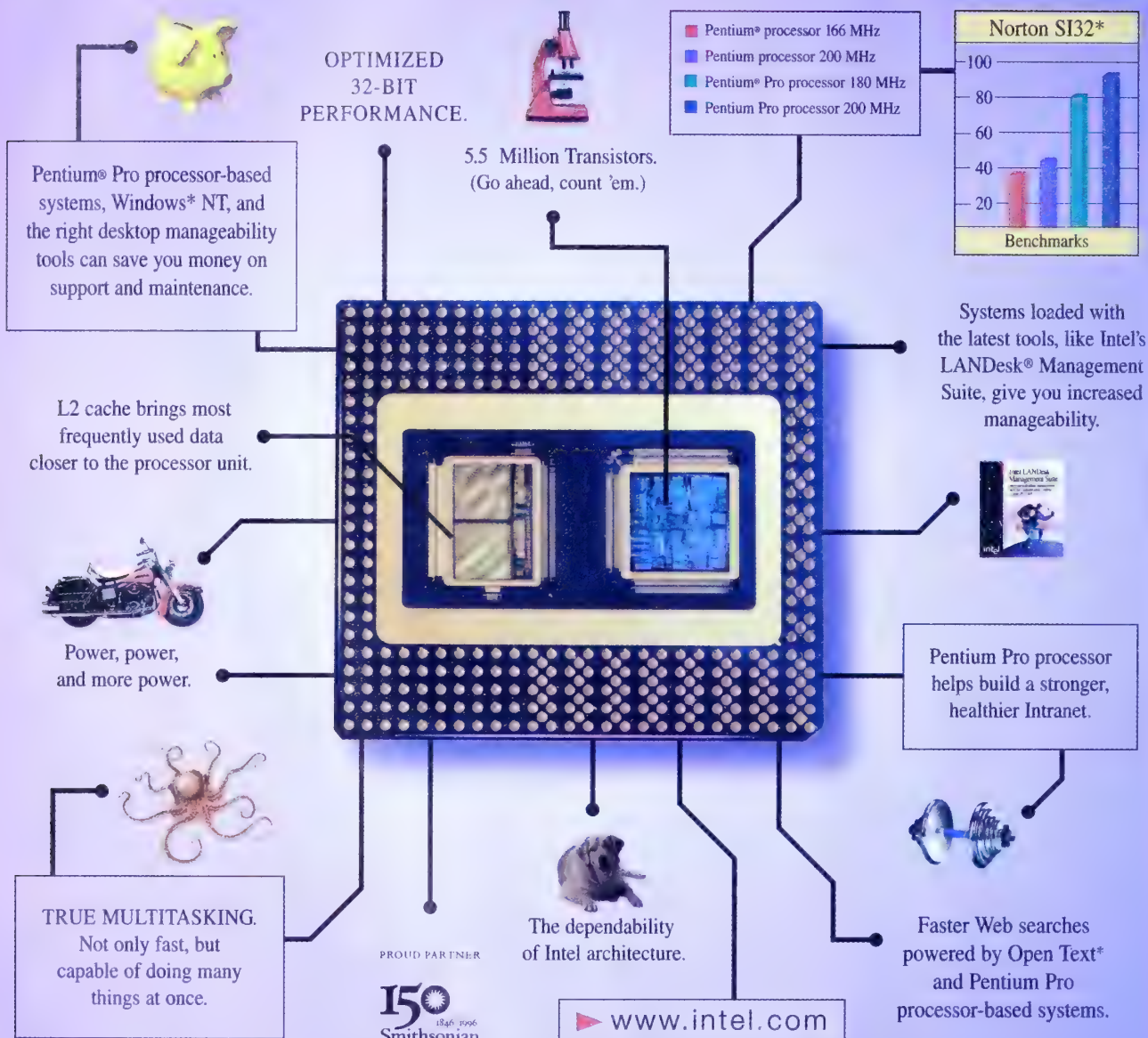
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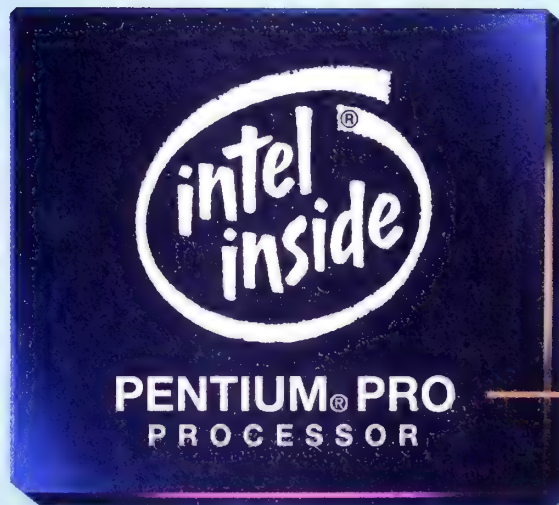
{ IT Overview }



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The Pentium® Pro processor

{ Executive Summary }



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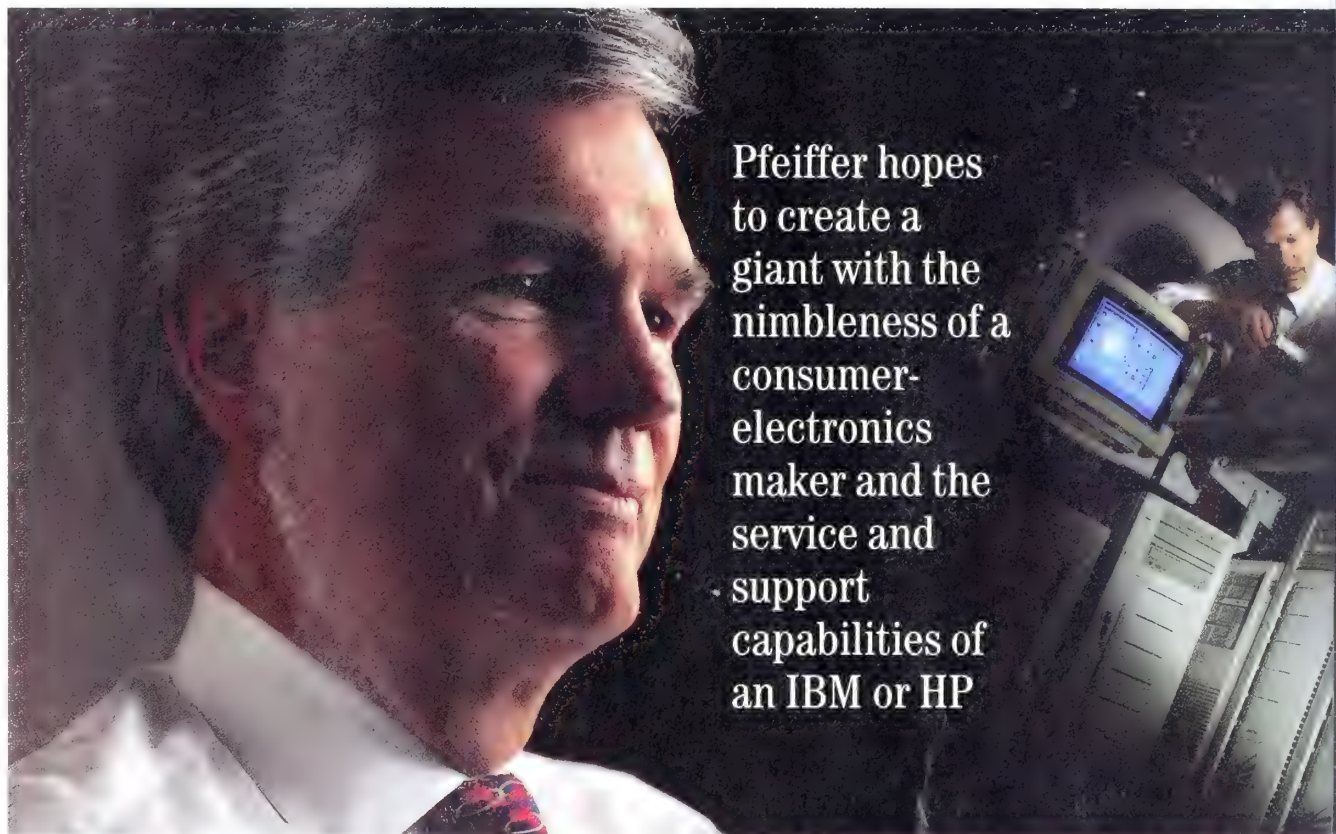
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COMPUTERS

COMPAQ AT THE 'CROSSROADS'

The computer maker is retooling again—and the boss is pushing hard for profits



Pfeiffer hopes to create a giant with the nimbleness of a consumer-electronics maker and the service and support capabilities of an IBM or HP

It was a close one. Faced with a sudden and totally unanticipated slowdown in sales, on Mar. 1, Compaq Computer Corp. Chief Executive Eckhard Pfeiffer was forced to warn analysts that the computer maker was unlikely to hit expected revenue and earnings for the quarter ending Mar. 31. The news sent Compaq's stock plummeting 18%, to 41%, in one day. After the announcement, Pfeiffer jumped into high gear. He ordered incentives for dealers and cut prices 20% to lift demand. It worked: Revenues for the March quarter jumped 42%. The stock quickly recovered most of its loss.

Pulling off such a save would be cause for celebration at most companies. But inside the \$14.8 billion PC giant, it was soul-searching time. The cost

of hitting Pfeiffer's growth target was a four-point drop in gross profit margin to 20.3%, its lowest ever and far short of the company's 23% to 24% goal. That exposed a troubling truth: For more than two years, Compaq has been running twice as fast only to stay in place—shipments and revenue have been hitting new highs, making it the world's top PC maker. But profits have barely budged.

It was time for a better formula. So on Apr. 15, Compaq drafted 20 managers from around the world for what became known as the "Crossroads" meeting. In a conference center at the company's Houston headquarters, Vice-President for Corporate Development Kenneth E. Kurtzman assembled five teams to tear apart Compaq's business-

es and assess each unit's strategy and that of key rivals. Three weeks later, the teams presented Pfeiffer with some sobering recommendations: Each business unit must be first or second in its market within three years—or Compaq should consider getting out of that line. Also, the company should no longer use profits from high-margin businesses to carry marginally profitable ones—each unit must show a return on investment. **FAST TRACK.** Fine. But Pfeiffer had his own requirement that would make achieving these goals a bit more complicated: Whatever happened, he insisted that the company remain on the superfast growth track that he laid out three years ago. Pfeiffer wants Compaq to keep growing at 20% to 25% a year, so that in 2000 it will be a \$40

billion behemoth and the No. 3 computer maker in the world, just behind IBM and Fujitsu Ltd.

Now, executives at Compaq have a new formula. To hit Pfeiffer's top-line targets, the company will move aggressively into all sorts of new product areas that will make it a full-line information-technology company—capable of competing across the board with companies such as IBM and Hewlett-Packard Co. On July 2, Pfeiffer announced a sweeping restructuring that created nine new divisions alongside the core desktop, laptop, and home-PC businesses. The new units will focus on fast-growing areas such as Internet



ALL SYSTEMS GO:
Compaq network servers at Smith-Kline Beecham

products and services, small-business systems, and engineering workstations. Pfeiffer also elevated a fledgling \$100 million networking-equipment business to a full division.

By yearend, Compaq will produce everything from computers for toddlers to mainframe-class servers able to run global financial networks. There will be powerful engineering workstations and lightning-quick network switches, too. Meanwhile, the company is stepping up its role as a venture capitalist, investing in companies with promising new products and technologies that can help the divisions compete—especially on the Internet (table, page 72).

"VIRTUALIZING." The second part of the formula—for producing profits along with growth—will involve wider use of outsourcing and partnership deals. That's because the new financial yardstick—return on assets—will force the divisions to slash investment in assets such as plant, inventory, and overhead wherever possible. If the \$3 billion home-PC business can cut its asset base, for instance, it can still deliver a 20% annual return to the company—even though price competition in home PCs will likely keep operating margins at around 2%.

To get there, Compaq has already started "virtualizing" parts of its business. After cutting \$57 off the cost of

each home PC last year by building the chassis at its plant in Shenzhen, China, the company went a step further in cutting the cost of business desktop PCs: Instead of investing millions to expand the Shenzhen plant, Gregory E. Petsch, senior vice-president for operations, persuaded a Taiwanese supplier to build a new factory adjacent to Compaq's to build the mechanicals for the business models. The best part of the deal: The Taiwanese supplier owns the inventory until it arrives at Compaq's door in Houston. "This is the right way to do it," says Sanford C. Bernstein & Co. computer analyst Vadim D. Zlotnikov.

By 1999, Pfeiffer expects each division to achieve best-in-class return on assets. PCs will have to better Gateway 2000 Inc.'s 21% return on assets, the networking business must beat 3Com Corp.'s 18% return, and workstations will have to top Sun Microsystems Inc.'s 14% return.

If the Crossroads plan is successful, Pfeiffer will have created the blueprint for the computer company of the next century: a giant with the nimbleness of a consumer-electronics maker and the all-encompassing service and support capabilities of big computer companies such as HP and IBM. "We're at a turning point in our company's history," says Pfeiffer.

The new plan will also involve a new regime. After living through the four-year growth sprint that took Compaq from \$4.1 billion in sales in 1991 to \$14.8 billion last year, Chief Financial Officer Daryl J. White resigned on May 29, citing "burnout." A month later, Systems Div. chief Gary Stimac, a key player in moving Compaq into its leading 40% share in PC servers, quit. "It would take another multiyear commitment in time and energy," says Stimac. "I had to evaluate my personal life." Meanwhile, industry reports have Senior Vice-President for

North America Ross Cooley resigning by yearend. Cooley, however, declined to comment.

For a few years, Pfeiffer has been assembling a new team of operations-savvy executives. The new CFO, Earl L. Mason, worked at Inland Steel Industries Inc. and Digital Equipment Corp. Michael J. Winkler, general manager of the PC Products Group, came to Compaq after a long career at Xerox and Toshiba America Information Systems. Consumer Group General Manager Michael D. Heil worked at Los Angeles Cellular Telephone Co. and Sony Corp. of America. Chief strategist Robert W. Stearns joined from McKinsey & Co.

"BIG IRON." One of the biggest jobs falls to John T. Rose, general manager of the enterprise computing group. Rose, a former DEC executive who joined three years ago, is responsible for pushing Compaq into "big iron" territory. With Intel Corp.'s new Pentium Pro chip and Microsoft Corp.'s industrial-strength

Windows NT, Compaq figures it finally can build the servers and workstations that can take on even the biggest computing jobs. The first such products are hitting the market now.

Compaq, already the top supplier of PC servers used in smaller networks, sees itself as the standard-bearer for the low-priced "Wintel" (Intel-based computers using Microsoft Windows software) technology as it sweeps into the last bastion of the mainframe and minicomputer. And some important customers agree. While IBM and HP are also promising powerful new Pentium Pro-based machines, buyers question whether those companies will push the technology as aggressively as Compaq, since the new setups can compete with their older, more profitable proprietary machines.

That's why Smith-Kline Beecham PLC chose Compaq over IBM and HP to supply the drugmaker's servers. "The big dif-



ference with these guys is they're intent on pulling this off," says Lou Valente, vice-president for North American information resources. "I don't see that intensity coming from other companies," he says.

To compete in the big-iron business profitably, Compaq is counting on a series of relationships with other companies that can supply the kind of hand-holding that companies such as IBM are famous for. Instead of investing in legions of field technicians and programmers—and building up costly assets—the computer maker will use the resources of systems integrator Andersen Consulting and software maker SAP, among others. These companies have the personnel to install and maintain systems the way IBM or HP do. So Compaq gets to play in the big-iron market without incurring the costs of running its own services or software businesses. Using these partners, Compaq is already delivering packages of networks, servers, and services to big customers including General Motors, British Telecommunications, First Interstate Bancorp, and Deutsche Bundespost.

Compaq, however, may not be able to play through their intermediaries forever. "The real solution is to create your own capability. It takes longer and is more painful, but ultimately, it is more successful," says Graham Kemp, president of G2 Research Inc.

Small and medium-size companies are also a key market for server technology. To reach them, Compaq will rely on its existing network of resellers. But it will give them new tools, including "blueprints" for installing and managing networks that can be applied in cookie-cutter fashion. "Our goal is to create a Compaq standard" for network and systems tasks, says Cooley.

KID STUFF. The powerful new Intel/Windows NT technology also provides Compaq with a chance to crack a small but lucrative new market: engineering workstations. While only about 900,000 workstations will be sold this year, vs. about 60 million PCs, profit margins are nearly twice as high. Sun, HP, Silicon Graphics, and others sold \$13.3 billion worth of such machines last year, and sales should expand at a 10% annual rate through the decade, says market researchers Dataquest/Gartner Group.

Meanwhile, Pfeiffer continues to push into fast-growing consumer markets. On July 15, the company will trot out an all-new line of home PCs. But the com-

pany has more than PCs in mind. And, again, Pfeiffer is counting on alliances to cut costs and provide expertise that Compaq can't duplicate. For example, the company is working with Mattel Inc.'s Fisher-Price Inc. to produce PC add-ons for small children. And a deal with Thomson Consumer Electronics Inc. is aimed at new hybrid computer/consumer-electronics products.

Pfeiffer also sees other opportunities for PC technology in the home. One of the biggest, he says, will be "home au-

making investments in Internet startups. It paid \$6 million in January for 7% of Raptor Systems Inc., a developer of security software for the Internet. Compaq is also a limited partner in Safe-guard Scientifics' \$40 million Internet Capital Group fund and in funds run by Kleiner Perkins Caufield & Byers, including one that backs startups using Sun's Java.

STRUGGLE. Pfeiffer's No. 1 objective on the Net is to make Compaq servers synonymous with so-called intranets. These networks use Internet technology within a corporation for things such as E-mail, employee communications, and electronic purchasing. Since February, Compaq has shipped Netscape's Commerce Server and Microsoft's Internet Information Server programs with all its server computers. "Compaq is ahead of everyone else in that space right now," says Forrester Research Inc. analyst Jon Oltzik.

The explosive growth of the Net will create unprecedented demand for servers and, perhaps, unprecedented competition. Compaq started early in PC servers and holds a commanding 40% market share, which has translated into healthy profit margins. Now, companies such as Dell Computer Corp. are hoping to make this a high-volume, commodity business—similar to desktop PCs. "Compaq is definitely going to lose some share," says HP Marketing Manager James P. McDonnell. "The question is how fast and how much."

Indeed, Wall Street worries that price pressure and market-share erosion in servers could hurt Compaq's earnings. Its stock has been trading recently at around \$46—well below its 52-week high of \$56.75. On July 17, analysts expect Compaq to report earnings for the June quarter about flat with last year's \$246 million.

Between the new competitive challenges and the new growth/profit formula, Pfeiffer certainly has taken on a huge job. But the 33-year computer-industry veteran is known for his tenacity. Once a goal has been set, he's not likely to fall short. Says Mentor Graphics Corp. Chief Executive Walden C. Rhines, a former colleague of Pfeiffer's at Texas Instruments Inc.: "I never, ever saw Eckhard miss a forecast. He'd sell the electricity out of the building before he'd miss a forecast." Pfeiffer will need all the juice in Houston to power Compaq through this next growth spurt.

By Gary McWilliams in Houston

Venture Capitalist

Where Compaq Is Investing

COMPANY	BUSINESS	DATE
BOOKS THAT WORK	Consumer software	Oct., 1994
MOBILEWARE	Wireless communications	Aug., 1992
NETWORTH	Networking switches	Nov. 1995
PURESPEECH	Speech-recognition software	June, 1995
RAPTOR SYSTEMS	Internet security software	Jan., 1996
THOMAS CONRAD	Network cards for PCs	Oct., 1995

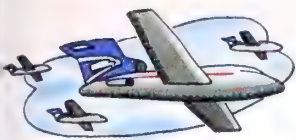
DATA: COMPAQ COMPUTER CORP.

tomation"—using computers to control air-conditioning, heating, and security systems. Pfeiffer has already pumped funds into startup Intellon Corp., which is developing chips for controlling everything from stereos to refrigerators from a PC.

The challenge in the consumer business, says Pfeiffer, is not finding new products and technologies to pursue but narrowing the focus to a manageable number. Even a \$15 billion giant such as Compaq could get distracted by taking on too much, he warns. "We see lots of opportunity. This field is growing so fast, there is a major challenge in reallocating our resources," says Pfeiffer.

One place he's not shy about placing resources, however, is in cyberspace. Despite a late start in the Internet, Compaq is looking to pick up speed by developing relationships with Internet software and service companies. On July 7, for example, it became the exclusive supplier of servers to Internet service company WebConnect Inc.

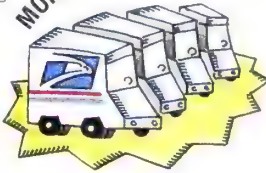
Compaq also has been aggressively



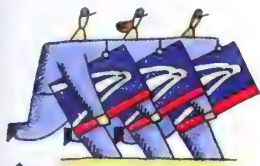
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THE GREAT EQUALIZER

74 BUSINESS WEEK / JULY 22, 1996

One reason why educational mobility might have risen is the enormous growth of the community college system over the last two decades. In 1970, two-year colleges accounted for about 27% of all college enrollment. Now, about 40% of college students are enrolled at community and other two-year colleges.

Statistics bear out the steady improvement in educational access. According to the Education Dept., about 45% of low-income high school graduates now enroll in higher education after graduation. That's up sharply from the levels of the early 1980s, when only 32% of them entered college.

To be sure, far more low-income students start college than finish it. "It's tough to keep them in," says former New Jersey Governor Thomas H. Kean, president of Drew University in Madison, N.J. "Anything that goes wrong—divorce, joblessness, any event—can throw off the calculation."

But people benefit from going to college, even if they never graduate. Economists Thomas J. Kane at the Council of Economic Advisers and Cecilia E. Rouse of Princeton University estimate that workers gain 4% to 6% in income for every year of college they complete, whether they achieve a degree or not.

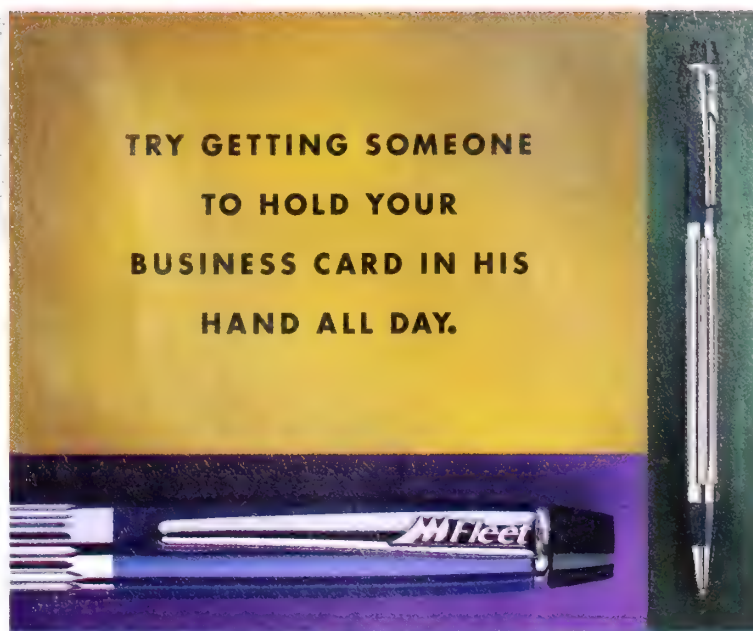
Even many kids from well-educated families fail to complete their degree. One government survey tracked students who entered college in the 1989-90 school year. Five years later, only 41% of those with college-educated parents had attained a bachelor's degree. About 24% had no degree and were no longer enrolled in school (the others either were still enrolled with no degree, or had a two-year degree).

FINANCIAL AID SQUEEZE. This shortfall may reflect the high and rising cost of college for middle-class families, who generally don't receive financial aid. "The kid from a middle-class family—that's the person who is really hurting," says Harold J. Raveche, president of Stevens Institute of Technology in Hoboken, N.J., where 43% of undergrads are first-generation students.

Cutbacks in state funding for higher education, combined with reductions in federal aid, are making it harder for both middle- and low-income students to stay in college. In response, President Clinton has proposed giving new tax credits and deductions for educational expenses, a measure that seems unlikely to pass in a time of deficit-cutting.

Even with tight budgets, America's higher education system is still able to open the door to upward mobility. In the long run, education remains the key to ensuring that the income divide does not become an uncrossable chasm.

By Michael J. Mandel in New York



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TURNAROUNDS

GETTING THE BUGS OUT

Now, CompUSA has other computer retailers on the run

When CompUSA CEO James F. Halpin invited Gordon B. Hoffstein, the head of direct-mail computer seller PCs Compleat, to dinner to discuss an alliance last December, Hoffstein accepted simply out of politeness. After all, he thought CompUSA Inc. was a troubled retailer with little to offer customers but a quick PC sale. "In no way, shape, or form were we going to sell our business to these guys," Hoffstein recalls.

Halfway into the dinner, Hoffstein had a change of heart. And in May, CompUSA, the nation's largest computer chain, acquired privately held PCs Compleat Inc. Hoffstein discovered what many PC users already knew: Today's CompUSA is far from the nearly bankrupt company of a few years ago. While shrinking PC margins and intense competition have short-circuited growth at rivals Best Buy Co. and Tandy Corp.'s Computer City, CompUSA is thriving. By bolstering complementary services such as computer training and using its base of more than 100 stores to support fast-growing sales to businesses and direct-mail buyers, the Dallas-based chain is barreling past its retail roots. "CompUSA has pros-

pered because Jim Halpin has thought beyond [the store]," says Alan C. Bush, the ex-president of Computer City who runs store operations for Dallas-based software chain NeoStar Retail Group Inc.

Just two years ago, CompUSA racked up a \$16.8 million loss on sales of \$2.1 billion. But for fiscal year '96, which ended in June, sales grew 30% over '95, to \$3.8 billion. Analyst David C. Childe of Salomon Brothers Inc. predicts income will more than double from last year, to \$56.7 million. That has made CompUSA a Wall Street star. From a split-adjusted low of 4 in August, 1994, its stock hit 47 in May before settling down to 34 as jittery investors reacted to slowing PC sales.

What's behind the turnaround? Under Halpin's predecessor, breakneck expansion coupled with poor controls and costly

TIGHT TEAM

Compton and Halpin have aggressively expanded into services such as training, installation, and repairs

moves into PC manufacturing and software publishing sent the company reeling. The board went looking for a replacement, and Halpin, the former CEO of HomeBase, an Irvine (Calif.) retailer, took over in late 1993.

Halpin soon replaced 17 of the top 20 executives. Among the recruits: Chief Operating Officer Harold F. Compton, whom he had worked with at HomeBase. A top-flight operations man, he and Halpin have

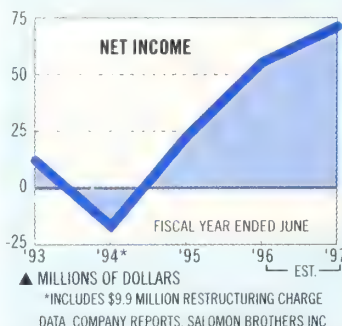
been a tight team ever since. "Jim is the visionary who can tell what changes need to be made," says James E. Skinner, CompUSA's CFO. "Hal makes sure [things] get done."

"INTERACTIVE." The two slashed costs, shuttered the unprofitable diversifications, and ended the rapid store growth. Then they fixed up the stores, which bring in 65% of sales. Increased training has ensured that staffers can talk tech with customers, for example, while new "try-before-you-buy" software kiosks have been a big hit. "CompUSA used to look like an old, tired record store," says Halpin. "We've made it an exciting, interactive place to shop."

With skidding PC prices putting pressure on margins, Halpin is now aggressively expanding into high-margin services where CompUSA can leverage its expertise. Although just an estimated 15% of revenues today, these services are growing fast. "When we deliver, install, and teach you how to use your computer, once it's sold, it stays sold," says Compton. "And the next time you're going to get a computer, we're very much at the top of your mind."

Computer training has been one big success so far. Although CompUSA had long offered classes, Halpin upgraded its offerings with a slew of new teachers and classrooms. Today, Compton claims it is the largest independent software trainer in the country. The success of in-store training led Halpin and

COMPUSA'S PROFITS RECOVER



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http://www.okidata.com

Omron Corp./North America
http://www.omron.co.jp

Oracle Corporation
http://www.oracle.com

Origin
http://www.origin.nl/

PageNet
http://www.pagenet.com

PeopleSoft
http://www.peoplesoft.com

The Principal Financial Group
http://www.principal.com

PSINet
http://www.psi.net/

Raytheon
http://www.raytheon.com

Roberts Express, Inc.
http://www.roberts.com

Charles Schwab
http://www.schwab.com

Saab
http://www.saabusa.com

SAP
http://www.sap.com

SAS Institute
http://www.sas.com/

Sequent Computer Systems, Inc.
http://www.sequent.com

Siemens
http://www.siemens.com

SkyTel
http://www.skytel.com

Sprint
http://www.sprint.com

Sun Microsystems
http://www.sun.com

Swissair
http://www.swissair.com

Symantec
http://www.symantec.com

T. Rowe Price
http://www.troweprice.com

Texas Instruments
http://www.ti.com

Toshiba America Information Systems
http://www.toshiba.com

Toyota Motors
http://www.toyota.com

Unisys
http://www.unisys.com

United Airlines
http://www.ual.com

U.S. Robotics
http://www.usr.com

UPS
http://www.ups.com

The Vanguard Group
http://www.vanguard.com

Wonderware Corporation
http://www.wonderware.com



Sun designed the
first intranet
back when people
thought intranet
was a typo.



http://www.sun.com

Compton to another hit. In January, CompUSA launched a delivery-and-set-up service. For \$79, the company will bring a PC to a buyer's home, install modems, and get software up and running. For \$70 more, CompUSA will also provide basic computer training at home.

The emphasis on training, combined with new services such as on-site repair, have helped CompUSA boost sales to small and midsize businesses. Halpin set up a sales force and warehouse for corporate buyers and added sophisticated services such as systems design and networking. Yet rivals question whether it can provide high-level technical support. "It's a stretch to say they can pull this off," says CompuCom CEO Edward R. Anderson.

"SOLUTIONS." So far, customers seem happy. At Dallas-based Dental Plan Inc., the country's largest provider of customized software for dentists, General Manager Jim Bennight turned to CompUSA because DPI needed support and training for 17,000 customers nationwide. He switched his buying from Dell Computer Corp. and IBM because "we just weren't getting the service. What CompUSA provided is total solutions."

Now, Halpin hopes to work the same magic in mail order. With the acquisition of PCs Compleat, CompUSA has become the nation's third-largest brand-name PC mail-order company. Customers with problems won't have to ship their computers back. "We provide mail-order convenience, but if something happens, you can take your computer to the closest store," says Compton.

With CompUSA on a roll, Halpin and Compton are once again adding stores. This year, CompUSA opened 20, and next year, it could open as many as 30. The pair is also aggressively pursuing acquisitions. But this time, investors appear not to be worried. Former Chairman Ronald N. Dubin says there's no comparison with the CompUSA of old. "For the longest time, we had the tiger by the tail, and the company was always scrambling to keep up," says Dubin, whose privately held investment firm, Dubin, Clark & Co., remains a large shareholder. "Management is now riding the tiger and controlling it."

Halpin, too, makes clear that the company isn't back to growth for growth's sake. "We're very sensitive about growth," he says. "In making acquisitions, you've got to kiss a lot of frogs before you get the prince." These days, CompUSA itself looks increasingly like one of those princes.

*By Stephanie Anderson Forest
in Dallas*

STRATEGIES

TWINKLE, TWINKLE, ECHOSTAR

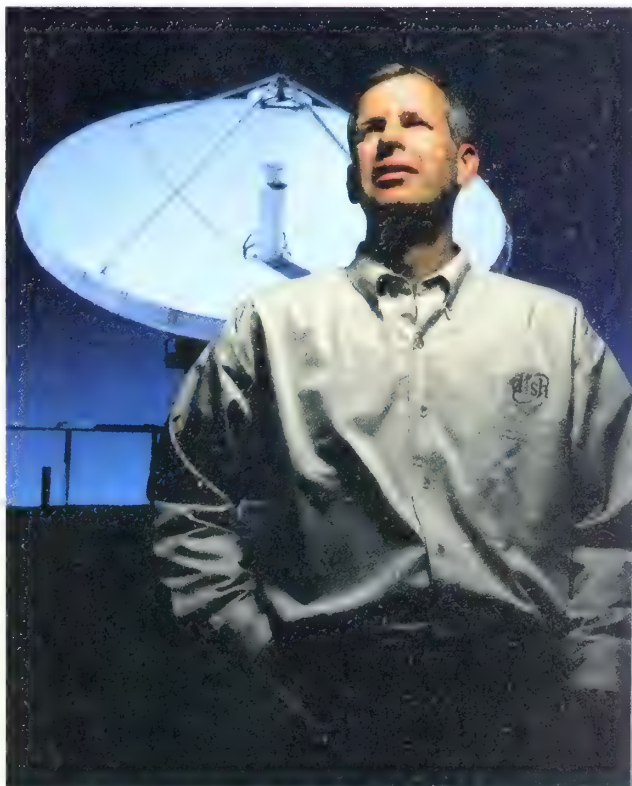
Can this upstart muscle in on AT&T and TCI in satellite TV?

Charles W. Ergen has had his share of tense moments, but nothing quite like this. For the past decade, he has struggled to start his DISH Network, the latest entrant in the market for digital satellite TV. Ergen survived rocket-launch delays, financing snafus, and countless mishaps. But one afternoon in June, Ergen's new \$50 million satellite-uplink facility in Cheyenne, Wyo. crashed. Complaints poured in from viewers facing blank screens. "It should never have happened," says Ergen.

The timing was bad, too. Ergen, the 43-year-old founder of EchoStar Communications Corp. in Englewood, Colo., is in the early days of a battle against such giants as AT&T, Hughes Electronics, and News Corp. Ergen faces a huge challenge: persuading viewers to watch their MTV, Disney Channel, and HBO movies on his little-known system.

CHEAPER GEAR. Although the uplink facility snarl-up was not serious, Ergen can ill afford missteps. He's joining the fight two years behind market leaders DirecTV, owned by Hughes and AT&T, and PrimeStar, controlled by a consortium of cable companies led by Telecommunications Inc. (TCI). For now, DirecTV and PrimeStar share a market of 3 million viewers that's projected to grow to 15 million by 2001.

Ergen may be coming in late, but he's not unarmed. By offering cheaper equipment and better deals on popular



"GUNG HO": By 1998, CEO Ergen sees 4 million DISH customers

programming than his big-name rivals. Ergen aims to snatch a sizable chunk of that market. Within 18 months, he hopes to have 1 million subscribers—enough to break even on an operating basis.

He's off to a fast start. Although the three-month-old broadcaster has only 75,000 viewers, a hot new promotional deal begun in June helped EchoStar attract 30,000 new subscribers that month. As he builds distribution, Ergen figures he can add the 60,000 monthly subscribers he needs to hit his target. Already, those plans are giving a jolt to the nascent digital-satellite industry. "Charlie is a very smart businessman," says Gary S. Howard, chief executive of TCI Satellite Entertainment Inc. "We're watching him closely."

Ergen's strategy is to drive a wedge between the upscale DirecTV service and the more affordable PrimeStar. DirecTV caters to viewers who ca-

plurge for up to \$800 in equipment costs and shell out as much as \$85 per month for an array of sports and movies. Primestar leases its large, unguaranteed dishes for \$10 monthly but provides more limited programs.

Ergen hopes to lure viewers away from both by selling his equipment at a loss—and making it up in programming revenues. With the June promotional offer, which Ergen is testing in eight cities, he began selling receiver-and-dish sets for just \$200 to those who signed up for a year. Ergen figures he can lose about \$150 on each set he sells. With roughly 50% margins on the \$300-a-year basic-programming packages, he'll be in the black on each subscriber after the first year. Ergen is also gunning for cable viewers. Wherever cable rates go up, Ergen moves in. The country is full of people who think they're paying too much for cable," he says.

So far, customers are taking Ergen's bait. "It was an easy decision," says Carol Serkowski of Broomfield, Colo., who signed onto the DISH Network in June. Although she preferred some DirecTV features, the deciding factor was price." Satellite dealers from Colorado to Maryland say EchoStar systems are outselling DirecTV 10 to 1. "We can't get enough of them," says Steve Stroel, owner of Satellite Showcase Inc. in Boulder, Colo.

It's too early to tell if Ergen's riskmanship will work. Analyst Rick Vesterman of UBS Securities Inc. estimates EchoStar will have a \$31 million cash loss for 1996 because of heavy start-up costs. If Ergen hits his 1 million-subscriber target by late 1997, cash flow should return to almost \$40 million. But competitors doubt that Ergen can afford his price cuts for long. "With Charlie, there's the smoke and hype, and then there's reality," says James Ramo, DirecTV's marketing head. "We don't think his strategy is sustainable."

4 ORBIT. Still, it's no small feat that Ergen, a wiry, kinetic man who favors faded blue jeans and well-worn, unlaced Nike high tops, has made it this far. A financial analyst by training, Ergen quit his job at PepsiCo Inc. at 25 because he disliked bureaucracy. An avid hiker, he moved to Colorado and founded EchoStar, which began as a retail dealership to sell the large satellite

systems then on the market. Working through 3,000 independent dealers, Ergen built a \$100 million company.

As the digital revolution and smaller dishes loomed on the horizon, Ergen realized he had to reposition. In 1987—with no outside financing and no idea how the emerging technology would evolve—Ergen filed with the Federal Communications Commission for the right to put his own satellite in orbit. By 1994, Ergen settled on a low-priced alternative to the new DirecTV service. He tapped the bond market for \$335 million to buy and launch two Lockheed Martin Corp. satellites.



stepped-up marketing plans in May. DirecTV will spend \$150 million alone this year, while AT&T will spend many millions more on a nationwide sales pitch to its 90 million customers. "Charlie is gung ho. He has been a visionary and a believer for a long time," says Michael J. Mahoney, a portfolio manager at G.T. Global Telecommunications Fund, which holds 1.5% of EchoStar's stock. "He's the Craig McCaw of this industry." Today, with 75% of the outstanding shares, Ergen's stake in EchoStar is worth around \$850 million.

But Ergen is far from home free. Although analyst Westerman estimates revenues will soar to \$348 million this

year, up from \$164 million, making money is another matter. Analysts say it will take EchoStar at least five years to turn a profit. Despite the DISH Network's brisk launch, Ergen still needs shelf space in national chains such as Circuit City Stores Inc. and Sears, Roebuck & Co. And unlike DirecTV, EchoStar has no tie-in with a big telecom company. Yet competition is heating up. In addition to DirecTV, MCI Communications Corp. has hooked up with News Corp. to launch a global digital system in 1998 called AskyB.

If Ergen is worried

about the big guns aimed his way, the scrappy fighter doesn't show it. Ergen says that a retail distribution deal is imminent and that he's negotiating to sell a slice of EchoStar to a major telecom outfit. (Industry insiders say he is talking to U S West Inc.) As for the AT&T campaign, Ergen thinks consumers will be smart enough to go for the better deal.

Still, Ergen's biggest problem is the race against time. In three years, \$1.3 billion in debt and deferred interest will start coming due. From less than \$24 million in 1995, interest payments will soar to \$155 million and more in 1998. Ergen must have 2 million subscribers by then to service the debt. He projects he'll be at 4 million. But with the industry undergoing rapid change, Wall Street is cautious. "The clock is ticking," says Westerman. Ergen has proved the doubters wrong before. For them, he has one message: Stay tuned.

By Eric Schine in Cheyenne, Wyo.

Satellite TV—What Consumers Get for their Money

	ECHOSTAR	PRIMESTAR	DIRECTV
EQUIPMENT COSTS	\$199*-\$799	\$10 monthly rental fee	\$499-\$949
PROGRAMMING OPTIONS FOR \$20 A MONTH	AMERICA'S TOP 40 40 channels, including Disney, MTV, Nickelodeon	No offerings	SELECT CHOICE 34 channels including TNT, Court TV, and pay-per-view movies
PROGRAMMING OPTIONS FOR \$30 A MONTH	PREMIUM PLUS 40 channels, plus choice of Cinemax, Showtime, HBO, or The Movie Channel	PRIME VALUE 63 channels include A&E, Disney, ESPN, regional sports	TOTAL CHOICE 70 channels include American Movie Classics and Disney; an extra \$25 for HBO

* Current promotional offer

DATA: COMPANY REPORTS, UBS SECURITIES, DBS INVESTOR

By the time EchoStar's first bird hit space, however, DirecTV had already been on the air for 18 months. Ergen insists the lag has had benefits. As a licensed DirecTV distributor, EchoStar studied its future rival closely. Ergen even went out on installation jobs to grill DirecTV customers—then got his small technical staff to improve EchoStar's offering. EchoStar's simplified on-screen guide came about because customers complained about DirecTV's complexity, for example. Ergen also built his uplink facility using the same architect DirecTV hired. But by building in low-cost Wyoming and using newer technology, Ergen cut costs in half.

That kind of maneuvering has helped woo investors. A June, 1995, initial public offering and another debt deal have raised \$400 million to fund two more satellites. After the IPO, EchoStar's shares quickly soared from 17 to 39—although they have fallen to around 27 since AT&T and DirecTV announced

OPTIONS FOR

Annie Hansley, a customer-service representative at Chemical Banking Corp., never owned stock or much cared about the market—until she received options, that is. In 1994, Chemical awarded Hansley and every other full-time employee “success shares,” or options to buy 500 shares of company stock at \$40.50 each. When the stock hit 50, 55, and 60, and stayed there for three days running, employees could exercise a portion of the options and collect the cash. Suddenly, checking the quote in the newspaper became an early-morning ritual at Chemical. And as the stock reached its target exercise prices and employees could cash out for a profit, the excitement reached a fever pitch. “I hadn’t been watching the stock price before. But once it hit 50, it was all we talked about in the morning,” says Hansley, who as a result of a 1996 merger now works in New York for Chase Manhattan Corp.

Like Hansley, millions of U.S. workers are learning for the first time what the options game is all about. That’s because stock options—once reserved for top executives and workers at high-tech startups that couldn’t afford to pay competitive

salaries—are filtering down to an ever-increasing number of

Cover Story

rank-and-file corporate employees. Since 1989, when pioneer PepsiCo Inc. granted every employee bonus options worth 10% of their salary, an estimated 2,000 companies have instituted their own broad-based option plans. Options are a productivity incentive for booksellers at newly public Borders, tellers at NationsBank, box packers at Pfizer, chemical-plant operators at Monsanto, baggage handlers at Delta Air Lines, and part-time espresso servers at Starbucks.

NO CHARGE. Even more companies are likely to use this incentive now that the Financial Accounting Standards Board (FASB) has settled a decade-old debate that kept many interested employers on the sidelines. In October, 1995, FASB determined that corporations didn’t have to take a charge against earnings for fixed-term options. In 1997, the projected cost of options need only be disclosed in a footnote to the annual report, allowing employers to expand their use of options with little direct impact on earnings.

In large part, the options boom is a product of downsizing and reengineering, which has compelled companies to rethink traditional compensation. Leaner companies rely on fewer employees to shoulder more of the work, while shareholders demand demonstrable links between pay and stock performance. So options are becoming a popular incentive in this new corporate culture that has left employees feeling disenfranchised because of mergers, acquisitions, and layoffs. “Options are an antidote to the stress and demoralization caused by restructuring,” says Robert Salwen, president of Executive Compensation Corp. in White Plains, N.Y. “And they’re a way for the company to acknowledge the greater role each of the survivors plays.”



NEW HOBBY “I hadn’t been watching the stock price before. But once it hit 50, it was all we talked about in the morning.”

— ANNIE HANSLEY

EVERYONE

Even line workers get them. Will they help companies grow?

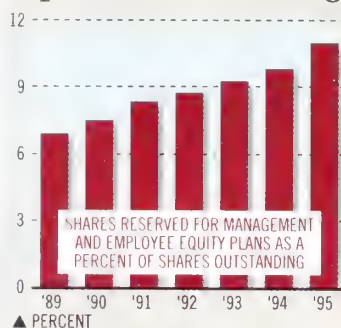


Indeed, companies hope that tying everyone to the stock price will inspire them to do their best to raise it. "We've been working for years to get the majority of our employees to hold company stock," says Sanford I. Weill, CEO of Travelers Group Inc., a diversified financial services company. The idea is to get everyone "to think like owners and build our wealth beyond what we would get in cash compensation." Upon discovering late last year that 26,000 of his 60,000 employees owned no Travelers stock despite opportunities to do so through 401(k) and employee stock-purchase plans, Weill announced in March that everyone with one year of service would receive an additional 10% of their compensation—up to \$40,000—in options starting in 1997.

Yet critics debate whether options are for everyone. How much impact can the average worker really have on the stock price? While companies with broad-based plans defend the growing number of shares set aside for option grants, it's still management that gets the lion's share. Hard numbers are sketchy so far, but even at companies that are sharing the wealth with more employees, few workers will enjoy gains anywhere near the \$41 million Weill's options reaped last year alone.

When the market's rise seems to be on auto pilot, and it's easy to make money, options appear to be a no-lose venture. But what happens when stocks inevitably cool? Many employees are market neophytes who have never bought and sold stock, much less experienced a correction. Companies argue employees have little to lose in a downturn since people only exercise if the stock price increases. And the risk of demoralization is tempered since most companies—for now, at least—have not reduced salary compensation when they debut broad-based plans. Yet countless new options holders may be in for a rude awakening when they realize the paper profits upon which they planned to retire have gone up in smoke.

Options Are Booming...



DATA: PEARL MEYER & PARTNERS

...As Employees Become Shareholders

Worker ownership of employers' stock, March, 1996

PLANS	EMPLOYEES (MILLIONS)	PLAN ASSETS (BILLIONS)
ESOPs AND STOCK BONUS	10	\$225
401(k)s (MAINLY HOLDING COMPANY STOCK)	2-3	200
STOCK OPTIONS*	3	100

* For plans that include most full-time employees
DATA: THE NATIONAL CENTER FOR EMPLOYEE OWNERSHIP

FRESH MIND-SET “ The idea is to get everyone to think like owners and build our wealth ”

— SANFORD WEILL

That's what happened to Wal-Mart Stores Inc. employees who depended on company stock—through profit sharing, a stock ownership plan, and options—for a large portion of their pay. When the stock tanked in 1994, those close to retirement cashed out at a fraction of what they had anticipated. The stagnant stock price caused morale to suffer among the rest of the workers, too. “It will be extremely interesting how companies explain to employees that all this money they thought they had disappeared in a bear market,” says Richard Semler, principal in the Los Angeles office of management consultant Sibson & Co.

Indeed, if companies don't educate their workforces about options risk, what looks like a magnanimous corporate gesture today could turn into a major employee-relations problem down the road—especially if workers ever forgo some of their salary for the perk. That's a big challenge when many workers are still grappling with how to invest their retirement savings through 401(k) plans. And there's an equally tortuous learning curve ahead for the growing number of options novices, who must acquire market savvy and self-discipline.

To be sure, many companies have been giving workers stock for decades, beginning with employee stock-ownership plans (ESOPs) and more recently through 401(k)s. However, ESOPs and 401(k)s usually must be held until retirement. Options are so alluring because they can be readily converted to cash, offering the prospect—and danger—of immediate gratification. This often proves tempting for people who view options as a quick money source instead of a long-term wealth builder, says Paul Allen, director of Smith Barney Inc.'s stock plan services.

PANIC TIME. A 1996 study by two associate accounting professors, Steven Huddart of Duke University and Mark Lang of the University of North Carolina at Chapel Hill, found that two-thirds of the exercise activity of lower-level employees occurs just six months after they are vested and the options are “in the money,” that is, when the market price is higher

than the grant price. Senior executives exercised at half that rate. Overall, 90% of

employees in the study sold their stock right after exercise. By doing so, the typical employee at the eight corporations in the sample sacrificed \$1 of expected value for every \$2 realized, Huddart and Lang estimate.

The experience of Chase's Hansley bears out those findings. Swept up in the excitement, she cashed out as many options as possible at the first two exercise prices. She figured she'd sit tight when the stock reached 60 and wait for it to move higher before exercising her last options. But when the price dipped slightly, she panicked and bailed out as soon as it inched back up to the low 60s. Since then, thanks to strong earnings, the bull market, and the merger, the stock has been as high as 74—and Hansley rues exercising early. “If I had a chance to do it again, I'd just hold onto them all,” she sighs. It would have been worth the wait: Those options would now be worth more than \$16,000 per employee, almost as much as a typical New York bank teller's annual salary.

So far, the gains employees have collected on options have been a valuable retention tool for companies. “When the market corrects itself, we'll see the value of options come back down to earth, but right now, they're an incentive for stay-



ing,” says Ray Harrison, senior information-systems manager at Network Equipment Technologies in Redwood City, Calif. “If you get a nice grant at review time, you think, ‘I might as well stick around till I'm vested.’”

Such thinking has benefited fast-food giant Wendy's International Inc. Before the launch of its We Share stock-option plan in 1989, restaurant crew turnover was almost 300% annually. “The main reason they left was frequent changes in management,” says Wendy's spokesman Denny Lynch. “So we had to do something to keep the managers to keep the crew.” Each year, everyone from assistant manager up gets

OWENS CORNING PLAYS SHARE THE WEALTH

“Come on, snake eyes,” shout workers huddled around a table at the Owens Corning plant in Huntingdon, Pa. Across the room, another calls back, “We're going to smoke your buns.” No, Owens Corning doesn't allow gambling. It's using a Monopoly-type board game to convince union leaders that adopting a variable compensation plan heavily dependent upon stock and options, is a good thing.

At Owens Corning, entitlement-style benefits are a thing of the past. Instead, effective Jan. 1, the 3,500 salaried U.S. employees became eligible for rewards, including nonqualified options, if the company achieves specific business results. Now it is selling the plan, Rewards & Resources, to union workers who make up the majority of the force.

From now on, three measures—earnings per share, cash flow, and sales growth—will determine long-term incentives for executives on down. Owens Corning is reducing its reliance on a retirement savings plan but adding a profit-sharing distribution of up to 4% of pay and an annual stock bonus of up to 8%, each linked to corporate performance. Employees also earn guaranteed yearly option grants of 4% of pay.

It's a radical change. “You're asking employees who have thought about long-term performance to do so actively,” says Greg Thomson, senior vice-president for human resources. Given the massive educational task, Owens Corning developed a board game to familiarize workers with key concepts.

The game, called Sharing the Wealth, was created by Coleman, a managing director at the Boston-based consu-

Cover Story

RISK 44 Employees may actually be de-motivated upon realizing that it can be like a lottery 77

— BOB GOWER

creased thanks to the rapid appreciation of their options, the benefit can be "tantamount to a bad marriage, since it can cost you too much to leave," says New York accountant Stuart Becker. Dave Hill, 40, a former senior manager at Reliastar Financial in Minneapolis, knows people who would like to leave their jobs but don't because they have too many unvested options. Five years ago, Hill passed up a great job offer for just those reasons. "It's very hard to look at your wife and say: 'I'm walking away from a six-figure amount,' knowing that all I'd have to do is stay there to get the money," he says.

The equity options generate can be a double-edged sword for employers. Thanks to patience and planning, Mike Greer, 45, was able to quit his job as the head of small-business banking at Cleveland's Society Corp. (now KeyCorp) and use the \$250,000 his options produced as the seed capital for his own business. Greer exercised his options incrementally as they reached target prices he set. When he resigned in 1991, he left behind thousands of options. In the years following, the bank merged twice and the stock went from the low teens to as high as 80. "I'm sure I gave up a substantial amount of money in continued appreciation to start my own business, but there was also no guarantee that I would have survived either of the bank's mergers," he says.

Some companies learn the hard way that distributing options

options equal to 10% of their previous year's earnings. Since 1989, turnover among assistant managers has dropped from 30% to 38%, and crew turnover has been cut almost in half.

Thomas Lee, 25, is one of those who stayed. An eight-year Wendy's veteran, he worked his way up from cook and cashier to assistant manager at Wendy's in Lebanon, Pa. Lee plans to use any options profits for the downpayment on a house. Wendy's assistant manager Sonia Murphy, 29, says the options she and her husband, a McDonald's Corp. assistant manager, receive have taught them the importance of saving.

But for executives whose net worth has dramatically in-

f Hammer and Co. The breaks down into six-per-ams, and each uses a separate game board to compete. By rolling the dice, players land on squares, choose a card, and make decisions with their team. For example, an "operating decision" has players debating whether to pull workers off the production line for job training. It's an up-front cost, but it pays off, savings will result. By doing it, rolling the dice determines how much they'll save. In life, luck plays a role. If a player hits a "crazy square" or a "luck card," they'll face an uncontrollable situation. In one scenario, a rival goes on strike, the plant picks up extra business. Each decision has a cost or benefit. The team with the best performance—and the biggest number of options awards—wins. Before playing the game, many workers were convinced Owens Corning was taking away benefits. There are a lot of skeptics, but they can't believe the company is giving us something good for free," said Rosalie Ryan, who has worked in the plant for 15 years, converting glass into fibers used in circuit boards. After the game, people said they had a better un-



STRATEGY: A board game helps employees grasp the subtleties

derstanding of the plan and their role in making it work.

As a reward for participating, each player received "starter options"—good for 10 shares of stock—exercisable only if the price hits targets during the year. If the workers apply what they've learned at the game board to their jobs, those starter options and future grants will be worth a lot more than Monopoly money.

By Kerry Capell in Huntingdon, Pa.

broadly is no panacea, even in a bull market. When Houston-based Lyondell Petrochemical Co. went public in 1989, all employees received a one-time option issue equal to 20% of their salary to buy the stock at \$30 a share. They could use payments from a profit-sharing plan to exercise the options. But for the past seven years, the stock has been trading mainly in the 20s, and the options have been underwater.

Lyondell CEO Bob G. Gower attributes the stock's poor performance to the cyclical nature of the industry. Although earnings have been relatively good—employees have received profit-sharing payments of 4% to 5% annually since 1989—the stock has been out of favor. “So many things can affect stock-price performance that have nothing to do with the individual employee,” Gower says. “Employees may actually be de-motivated upon realizing that it can be like a lottery.” That’s why Gower prefers profit-sharing plans, which keep workers focused on earnings instead of the share price. “We should only ask employees to control things they can influence, like earnings,” he says.

Some companies, such as Owens Corning, are looking for ways to use broad-based option plans but link them more closely to good performance. As the current bull market has shown, even companies with mediocre results have seen big jumps in share prices and options values. (Since early 1989, the total return of the Standard & Poor’s 500-stock index has been 181%.) So some activist shareholders argue that the exercise prices for options should be pegged only to ambitious increases in the stock price or other benchmarks. Such premium-priced or indexed options would ensure that employees benefit only to the extent that the stock outperforms the market or its peers.

BACKLASH? Some sophisticated shareholders question if options are really the “free money” that many executives claim they are. They fret that setting aside massive amounts of outstanding shares will dilute earnings, hurting existing stockholders. Today, about 10% of shares outstanding are reserved for option grants at companies such as Toys ‘R’ Us Inc. and Pfizer Inc. But it can be much higher: Morgan Stanley & Co. requested shareholders’ approval to allocate 55% of outstanding shares for its 1996 stock-option plan, bringing total potential dilution from employee options to 73%, according to the Investor Responsibility Research Center (IRRC) in Washington. Morgan Stanley shareholders had little trouble supporting the plan: Current and former employees own 33% of the company.

The potential for increased dilution may be fueling a backlash. The percent of shares voting against new stock-option plans was 17.3% as of 1995, a fivefold increase since 1988, the IRRC reports. “I’m absolutely convinced that number will increase as shareholders understand the issue better,” says Nell Minow, managing director of LENS, an activist money manager in Washington. With shareholders sensitive to dilution, one of the most delicate balancing acts companies face is

determining eligibility, says Peter T. Chingos, head of compensation consulting at KPMG Peat Marwick. Supermarket chain Safeway Inc. issues stock-option grants primarily to store managers and above. “With 114,000 employees and only 240 million shares outstanding, it’s very difficult to give a meaningful amount of stock to everyone,” explains CEO Steven A. Burd. “You have to make some choices about how far down in the organization you take it.”

Proponents contend that fears of excessive dilution are unfounded. First, the number of options exercised each year is small relative to total shares outstanding. Dilution at PepsiCo and DuPont Co. is around 1% of outstanding shares, says Matt Ward, a stock-compensation expert at Watson Wyatt in San Francisco. And options are exercised only if the stock price has gone up. Besides, they argue, the income gained from

the exercise of options and the corporate tax deductions from nonqualified options can be plowed into repurchasing shares to neutralize dilution. General Mills Inc. repurchases shares at prices lower than the ultimate exercise price, which helps control costs, claims Alan J. Ritchie, vice-president for compensation and benefits at General Mills in Golden Valley, Minn.

FEW NUMBERS. Many companies believe sharing options wealth is a good first step toward bridging the gap between shareholder returns and growth in employee wages and benefits. In 1995, return to shareholders was above 37%, while employees got less than a 3% increase in pay and benefits, says compensation consultant Frederic W. Cook. To combat the ire this might generate, he suggests increasing the amount of acceptable dilution to 20% from 10%, and the number of employees eligible to participate in options plans.

Surprisingly, many companies don’t seem to keep hard numbers quantifying options plans’ successes. “We knew going into it there was no way to prove the benefit to the company, but we believed very strongly it was a good idea,” says PepsiCo spokesman Richard Detwiler. Adds Ward: “The benefits are so obvious, it’s hardly

worth the time and money to calculate them.”

Luckily, today’s corporations pushing options well down into the organization can take some cues from long-time options users in the high-tech industries, notes Salwen. First, keep the broad-based plan simpler than that for executives. Use only plain-vanilla options and clearly defined vesting periods. Second, don’t issue token grants: Make sure the awards are financially significant to the recipients. Third, he says, it’s not enough to make employees stock owners. Companies need to create an environment that allows people to act like owners, too.

If properly implemented and communicated, options can be a great equalizer, says General Mills’ Ritchie. But if companies and workers don’t plan for both the risk and reward, there won’t be any real winners in the options game.

By Kerry Capell in New York



GONE 44 I'm sure I gave up a substantial amount of money in continued appreciation **77**

— MIKE GREER

O.K., YOU HAVE THE OPTIONS. NOW WHAT?

How to make the stock options granted by your company work best for you

So the company has finally recognized how valuable you are and given you stock options. You're a player; you've earned this reward. But after the novelty fades, you feel a sense of dread as you ask yourself that nagging question: What the hell do I do with these?

Whether you spend your days toiling in a cubicle or kicking back in the corner office, consider your options an investment to be managed rather than found money. You're an investor now, so start thinking like a stock analyst.

First, take a cold, hard look at both the company's prospects and your own. You'll need more insight into your company than the latest gossip around the watercooler. How competitive is it? Check the library for research from independent rating services such as Value Line Inc. Scan the newspaper stock listings for the price-earnings ratio and compare it with those of industry peers. If it is much higher, the stock may be overvalued; a lot lower, there's probably room to grow. Armed with those basics, you may want to call your broker and find out the firm's outlook for the stock.

After you get a handle on the company's future, start thinking about your own. How you play the options game will depend on the type and number of options you receive

as well as on your personal financial situation and investment needs. Many lower-level employees with limited disposable income will use the option program for a quick cash-out, since raising the money to buy and hold the stock often isn't feasible. But if you have a lot of options and a higher income—and thus greater tax liability—more intricate planning is required. "Most people, including the highest-paid executives, don't fully appreciate the value of their options, so they don't develop a strategy to exercise them," says Richard Friedman, vice-president for the employee benefits group at Ayco Co., an executive financial planning firm in Albany, N. Y.

Getting the most mileage out of your options means first decoding the optionese (page 88). "There was so much jargon on the grant form describing the options that I didn't understand what they were," recalls Lynda Ollinger, a 33-year-old senior executive administrative assistant with AEGON USA Inc. in Cedar Rapids, Iowa. Since she received her first grant seven years ago, the stock price has quadrupled. Now a virtual stock market junkie, Ollinger has formed an investment club with 21 co-workers.

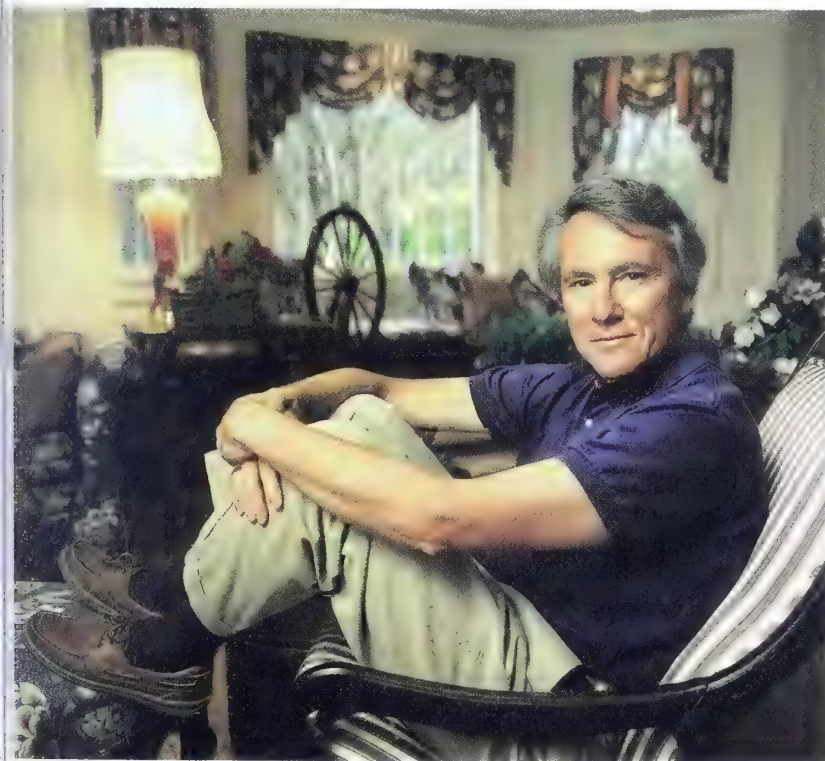
Most people receive nonqualified options—so called because they don't merit special tax treatment—which are granted at a fixed exercise price. Usually one year from the date of the grant, a percentage of your options is vested, or exercisable. At that time, as long as the current stock price is above the grant price, you may exercise your options—often just by placing a call to your company's benefits office. With nonqualified options, any appreciation above the grant price is taxed as

A Practical Guide

- ▶ How to value options
- ▶ Exercising your grants
- ▶ When to cash out
- ▶ How they're taxed

TIMING “People need to get money from their options off the table before it’s too late”

— LOUIS GAGLIANO



"If you don't think about what you're going to do until s

ordinary income, which you must pay at the time you exercise. That spread is tax-deductible for companies—one of the main reasons they prefer to grant nonqualified options.

However, you'll need to come up with the cash to cover both the share price and taxes when you exercise nonqualified

options. To avoid having to deplete your savings, most people use a cashless exercise. Many companies—including DuPont, Merck, Toys 'R' Us, Warner-Lambert, and Wendy's—work with a recommended list of brokerage firms. You simply call the plan administrator, who notifies the broker. That broker

then buys and immediately sells enough shares to cover the stock purchase, taxes, and commissions. Commissions vary and in many cases are negotiable, especially if you exercise and sell large blocks of shares. Since you'll technically be borrowing the cash to purchase the shares while the transaction is handled, you'll also pay the broker's margin rate for a minimum of three days. Any remaining shares can be sold for a cash profit or held. If you hold the stock, any future appreciation is taxed as capital gains when you eventually sell.

For transactions of fewer than 5,000 shares, it makes sense to use the company's recommended broker, if available, since the commissions are comparable and the execution is often faster. The first time Network Equipment Technologies information systems manager Ray Harrison, 46, wanted to exercise his options, he used his own broker. In the several days it took his broker to reach NET's plan administrator, the stock fell two points, costing Harrison \$3,000. Now he goes to the company's suggested broker. Although trades must be settled in a minimum of three days, the approval process that occurs before the trade can take place may take longer, as it did in Harrison's case. **SHOP AROUND.** If you have 5,000 or more options to exercise or you don't have the luxury of a company-affiliated broker, you'll need to comparison-shop. Discount brokerages aren't always the cheapest. On blocks of stock in excess of 5,000 shares, expect to pay from 5¢ to 25¢ a share in commissions. It is also essential to understand the firm's execution capabilities, because fractions of a point can make a big difference, says Gerry Klingman, a financial adviser with Robert W. Baird & Co. in New York. And find out whether the firm has worked with other employees at your company to exercise options, since its brokers will be familiar with the plan's provisions and the administrator minimizing time spent on approval.

Incentive stock options, or ISOs—usually reserved for upper-level executives—work much the same way as nonqualifieds, with a few notable exceptions. The beauty of ISOs is that no tax is owed at the time of exercise; more important, if the stock is held for at least one year from exercise and two years from the grant date, any appreciation when the stock is sold is taxed as capital gain rather than regular income. Because of this tax advantage, companies may grant only up to \$100,000 in ISOs per employee each year. So most top management

Cashing Out...

CONSIDER EXERCISING IF...

- ▶ Your options are in-the-money—when the current share price is greater than the exercise price—and about to expire.
- ▶ Your job is not secure or you're thinking about retiring or leaving, and the options expire upon or shortly after your termination.
- ▶ The options are your only source of cash to meet an immediate need such as college tuition payments or a wedding.
- ▶ You're confident the stock has peaked.

HERE'S HOW TO DO IT

- ▶ **CASHLESS EXERCISE** Your broker will lend you the money to exercise, then immediately sell enough stock to cover the exercise price, commission, and taxes; you keep whatever is left over in cash or stock. This is the most popular method because you don't need any cash up front.
- ▶ **MARGIN LOAN** Your broker can help you borrow as much as 50% of the value of your investment portfolio, or the options themselves pending delivery, to buy the stock. Rates will hover around prime.
- ▶ **STOCK SALE** Sell shares of any stock you already own, pay capital gains, and use the remainder to exercise options.
- ▶ **STOCK-FOR-STOCK SWAP** This exchange lets you use company shares you already own—deferring capital gains on any profit—as "cash" to exercise the option. You turn in the number of shares worth the option price to your employer now. Capital-gains tax is due whenever you sell. The same tax treatment applies to your options as if you exercised with cash.

DATA: STEPHEN PENNACCHIO, KPMG PEAT MARWICK

...and Paying Uncle Sam

SITUATION	EMPLOYEE	COMPANY
NONQUALIFIED OPTION		
OPTION GRANTED	No tax	No deduction
OPTION EXERCISED	Difference between grant price and current market value taxed as ordinary income	That same spread deducted as compensation expense
STOCK SOLD	Post-exercise appreciation or decline taxed as capital gain or loss	No deduction
INCENTIVE STOCK OPTION (ISO)		
OPTION GRANTED	No tax	No deduction
OPTION EXERCISED	No tax unless federal alternative minimum tax applies	No deduction
STOCK SOLD	Difference between exercise and sale price taxed as capital gain	No deduction

DATA: CONFERENCE BOARD, ROBERT SALWEN, EXECUTIVE COMPENSATION CORP

Months from retirement, you don't have many choices"

equity compensation still comes from nonqualified options.

With nonqualifieds, the conventional wisdom is to wait as long as possible to exercise, assuming you're confident about the company's future growth. Don't panic if the value of your options sinks "underwater" (when the stock price falls below the grant price) early on. When British Petroleum Co.'s stock dropped to the low 50s in 1992 as a result of plummeting oil prices, BP attorney Lynne Alfred, 54, watched years of options become worthless. When her options finally became exercisable two years later as the stock climbed back into the 60s, Alfred decided to wait. Perseverance paid off: She cashed out most of her options in 1995 in the low 80s and the rest on her retirement in February, when the stock jumped to more than 100. Since most options expire 10 years from the grant date, it usually doesn't make sense to cash out the first time the stock recovers after a dip. "If you look back over any 10-year period, the market tends to correct itself," says Peter T. Chingos, head of compensation consulting for KPMG Peat Marwick in New York.

Still, many people are tempted to cash out early to buy a house or pay college tuition when, in the case of rapidly appreciating stock prices, they might be better off holding on to their options and taking out a personal or home-equity loan. Depending on the number of options and how well the stock performs, the gain—which is tax-deferred—could more than cover any loan and interest payments, says Klingman of Baird.

But the idea isn't just to close your eyes and hope for the best. Your personal situation may require you to start exercising early. For example, if you have good reason to believe the stock is undervalued, consider exercising as soon as you're vested and holding the stock until the price is near its peak, says Minneapolis financial planner Ross Levin. That way you'll pay ordinary income taxes on the relatively small amount of appreciation accrued the year after the grant, and all subsequent gain will be taxed at a lower capital-gains rate when you sell. Or if you plan to move from a state with low or no income tax, it makes sense to start exercising nonqualified options before you go.

SET A TARGET. Similarly, if you're thinking about leaving the company, develop a game plan well in advance. "If you don't think about what you're going to do with the options until you're six months away from retirement or a new job, you don't have many choices left," says Karen Spero, of Spero-Smith Investment Advisers in Cleveland. Exercising nonqualified options incrementally helps ensure that you aren't forced to cash out all your options at once—which could push you into a higher tax bracket—or leave some on the table.

That's why it's a good idea to set target exit prices for each of your grants. Most companies give former employees up to three months after leaving to exercise, but you should always check with the plan administrator. Not paying attention to such details caused Richard Gillman, a former top executive at Bally Manufacturing Corp., to forfeit more than \$7 million in stock options. Gillman, who waited to exercise until 16 days after the company's one-year post-retirement exercise period ended, took the company to court twice and lost.

Even with professional help, you must be vigilant. When he

first began receiving options in 1984, Louis Gagliano, then a vice-president for internal audit at U.S. Surgical Corp. in Norwalk, Conn., was already planning an early retirement. On paper, he became a millionaire many times over. "It seemed like there was no top to the stock price," he recalls. Strapped for time and frequently traveling, he hired a financial adviser at a well-known money-management firm to watch the stock. Unfortunately, that adviser and a subsequent money manager neglected to develop a strategy to help disentangle him from his options.

It was the start of an emotional roller coaster. Gagliano watched the stock price plummet after the announcement of a Securities & Exchange Commission investigation and then soar after a few technological breakthroughs. The share price

Cover Story

So, How Much Are They Worth?

HOW THE PROS DO IT Traders often use the Black-Scholes option pricing model to calculate the value of short-term exchange-traded options. It incorporates such variables as stock-price volatility, interest rates, dividend yield, the difference between the stock's price and the options' strike price, and the time until expiration. You can find the formula in finance texts, or ask your broker.

A LAYMAN'S SHORTCUT For companies with average stock price volatility, 10-year options, and an average dividend yield, the Black-Scholes option value is typically 33% of the price of the optioned stock on the date of the grant (e.g., \$33 for a \$100 stock). The percentage may be above 50% for highly volatile stocks with low to no dividends or 25% or less for less volatile stocks with higher dividend yields.

THE EASIEST WAY Here's how you can project the gain: Say you receive 10-year options on \$1,000 of stock today. Assuming that the stock will grow 10% a year (based on historical performance) over the decade, the optioned shares will be worth approximately \$2,600 ($\$1,000 \times 110\%$ annually for 10 years). Then subtract the \$1,000 option price from the \$2,600 value, yielding a \$1,600 gain. Next, add the 10-year Treasury yield (approximately 7%) to an equity risk premium of 6% (13%). Finally, find the present value of the \$1,600 gain by using the 13% discount rate ($\$1,600$ divided by 1.13, 10 times). That works out to \$471, or 29%.

DATA: ROBERT SALWEN, EXECUTIVE COMPENSATION CORP.

seesawed from 4 a share in 1984 to 110 in 1991 before crashing back to 19 three years later. Although Gagliano, 51, retired two years ago on the millions his options generated, he knows it is just a fraction of what he could have earned. "People need to be self-disciplined enough to get money from their options off the table before it's too late," Gagliano says.

That's why financial planners advise you not tie up too much of your net worth in company stock through options, 401(k) plans, and other vehicles. Otherwise, even a small movement in the shares could dramatically affect your portfolio and net worth. Professionally managed mutual funds allocate no more than 5% to one security. While it's not always possible, especially at the executive level, people should make an effort to keep their exposure to company stock under 10%, advises Klingman. One solution if you have a trove of options: reduce company stock holdings within your 401(k).

With ISOs, the timing and the means of exercise is different,

The alternative minimum tax can give those who exercise options unwisely an ugly surprise

especially for those in higher marginal tax brackets. Here, a cashless exercise isn't always appropriate, since it defeats the main tax advantage of ISOs, says financial planner Levin. By selling portions of the stock—as in a cashless exercise—instead of holding ISOs for the required year, you pay income tax on the appreciated value. And while you could sell shares

you already own to exercise the options, you would have to pay capital gains.

Cover Story

Instead, ISO owners are better off buying the shares directly or making a tax-free exchange of company stock they already own to exercise the options. Such a stock-for-stock swap lets cash-strapped employees exercise options they might otherwise have let lapse. The company gets the stock and you receive the shares from the exercised options. The beauty of the technique is that the Internal Revenue Service lets you defer capital gains on the original stock you swapped.

A combination of strategies may work best. Kenneth H. Thorn, an executive vice-president at the former First Fidelity Bancorp, had to exercise 50,000 options—nonqualified and ISOs—before they expired. Using a cashless transaction, he exercised and sold his nonqualifieds, investing the proceeds in mutual funds. To acquire his ISOs, he swapped other shares he already owned and took a margin loan pending delivery of the ISO shares to his brokerage account. Many people don't know that they need not sell the securities immediately, as in a cashless exercise, but can maintain a margin loan of up to 50% of the shares' value. When First Fidelity was acquired by First Union Bank, an additional 30,000 options became exercisable. Thorn used the proceeds from the cashless exercise of those options to pay off his margin loan. "The advantage was that he was able to exercise his nonqualified options without using cash, diversify his holdings, and still retain his shares from the ISOs, which have now appreciated even more," says Klingman, his financial adviser.

UNCLE IS WAITING. ISO owners might also want to consider exercising early and then holding if the optioned stock is rapidly appreciating and has a reasonable dividend. The bull market makes this strategy especially attractive. It's not uncommon for stocks to have appreciated nearly four times their original value during the 10-year option term. In that case, a stock paying a modest 2% dividend will yield an 8% return on the cash required to exercise. Those dividends may also be sufficient to cover the carrying costs of a margin loan used to exercise the ISOs.

But be warned: Exercising and holding a lot of ISOs in any one year could expose you to the alternative minimum tax (AMT), a separate calculation to ensure that taxpayers with special deductions will pay at least some tax to Uncle Sam. (Nonqualified options aren't subject to the AMT because there's no deferral; all the gains are realized at exercise.) "It's important to run tax projections before exercising ISOs to ensure that the AMT doesn't make the tax benefits of ISOs somewhat illusory," Levin says.

Steve Pennacchio, a partner at KPMG Peat Marwick in New York, tells of an executive who turned to a small tax preparer for help with his ISOs. Told that it wouldn't be a problem, he exercised all of them at once, inadvertently creating a \$120,000 AMT exposure. "It could have been avoided by staggering the exercises," says Pennacchio. Indeed, making your options work can be a fruitful exercise, once you understand the rules.

By Kerry Capell in New York

An Options Primer

Options can range from the plain vanilla to the ultra-esoteric. Here's how to make sense of the Babel.

INCENTIVE STOCK OPTIONS (ISOs) An option that qualifies for favorable tax treatment as long as you hold the shares for two years after the grant and one year after exercise. Any gain realized from the time of the grant to the time of the sale is taxed as capital gains.

INDEXED OPTION An option to buy company stock with an exercise price that periodically adjusts upward or downward in relation to market or industry indicators.

IN-THE-MONEY OPTION An option where the current share price is greater than the exercise price.

MEGA-GRANT A large, usually one-time grant of options or shares to top executives that can be as much as three to five times the size of a normal grant.

LEVERAGED OPTION A plan promoting share ownership. For each share of company stock held or invested, the employee receives a certain number of additional options. Also, an option plan where the number of shares exercised increases based on stock-price movement or other financial performance.

NONQUALIFIED STOCK OPTION When you exercise this option and purchase the shares, the difference between the price paid for the stock and the fair market value at the time of exercise is taxed as ordinary income. When you sell the stock, any subsequent appreciation is taxed as capital gains.

PERFORMANCE OPTION An option where the grant, exercise price, or vesting is contingent on the company achieving financial or other goals.

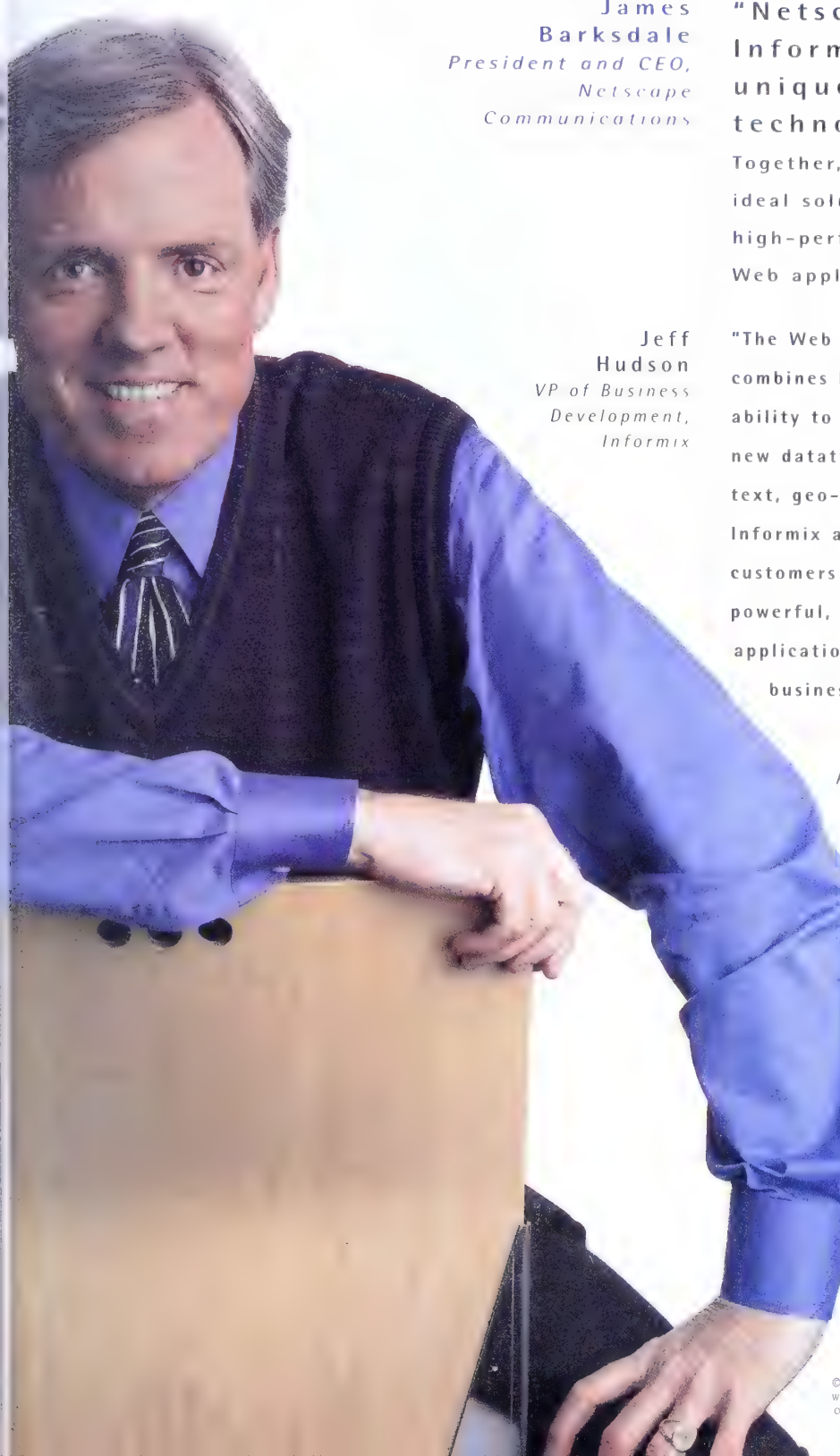
PHANTOM STOCK The next best thing for employees in certain countries where options aren't permitted. It consists of units equal to the fair market value, book value, or a formula price at the date of grant. At a specified future date, the employee is paid the appreciation in the value of the units.

RELOAD OPTION An option to buy company stock that is granted with the provision that upon exercise, if the exercise price is paid in previously owned shares, a new option is automatically granted for the number of shares used in the exercise.

STOCK-APPRECIATION RIGHT An award paid in cash or shares that gives the employee the appreciation on the stock from the time of award to the exercise date. When granted in tandem with options, the exercise of the stock-appreciation right cancels the option.

UNDERWATER OR "JACQUES COUSTEAU" OPTION An option that has lost value because the current market price has fallen below the original exercise price.

Netscape's James Barksdale on Informix.



**James
Barksdale**
*President and CEO,
Netscape
Communications*

**Jeff
Hudson**
*VP of Business
Development,
Informix*

"Netscape partners with Informix because of its unique Web database technology.

Together, we provide customers an ideal solution for next-generation, high-performance, content-rich Web applications."

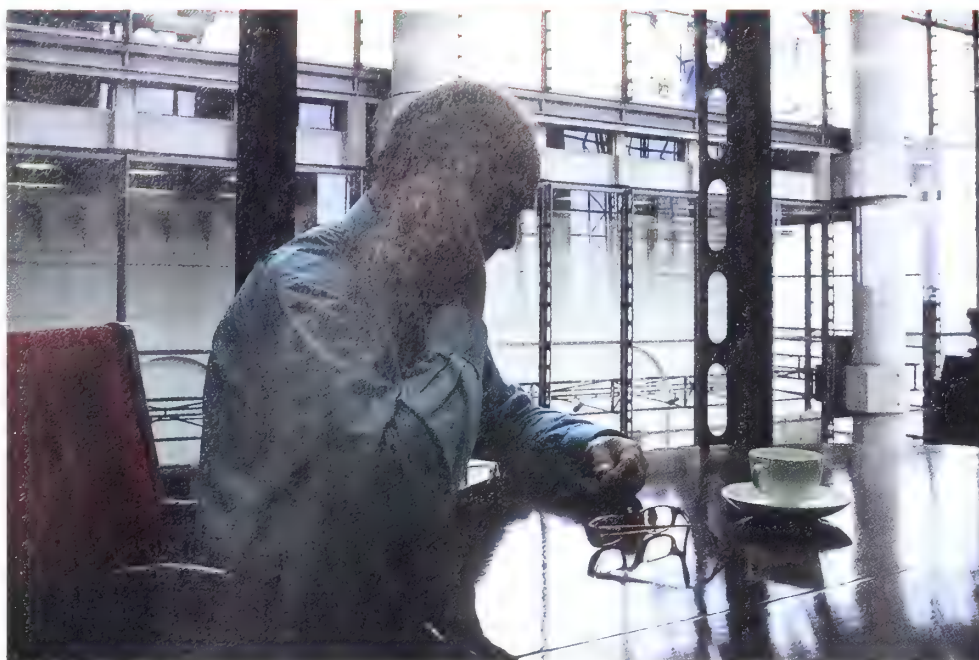
"The Web requires a database that combines high performance with the ability to manage a wide range of new datatypes—image, video, text, geo-spatial, and more. Informix and Netscape enable customers to quickly develop powerful, innovative Web applications that meet any business requirement."



At Informix, we deliver innovative database technology for a growing number of industry leaders worldwide. By teaming with companies who share our vision, we provide our customers with the solutions they need to stay ahead of change, make the most of emerging opportunities, and gain a competitive edge in business.

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CRUNCH TIME: Rowland must convince regulators Lloyd's has the capital to stay afloat

reached an agreement in principle in early July, insiders say. But the U.S. negotiators still need to sell the deal at home. Unless Lloyd's can convince U.S. investors to accept the offer and drop their lawsuits, the rescue plan could fail. "It is still possible that Lloyd's could collapse," concedes Chairman David Rowland.

"ABSOLUTE CHAOS." There's no time to spare. Lloyd's faces an Aug. 28 deadline to prove to British regulators that it has sufficient capital to stay in business. Otherwise, they could declare it insolvent. That, say industry participants, could produce an industrywide meltdown. Since most big insurers

lay off risks by reinsuring at Lloyd's, a collapse could be "absolute chaos," says New York State Insurance Superintendent Edward J. Muhl.

Even if Lloyd's makes it through this minefield, the 308-year-old market faces a severe competitive threat. It's still unclear whether it will be able to match a horde of more venturesome rivals unencumbered by Lloyd's unwieldy, high cost, outdated structure.

More immediately, the rescue plan is probably the exchange's only hope. It would create a separate company, Equitas, to reinsure Lloyd's heavy pre-1993 losses. That would allow Lloyd's to continue underwriting.

So far, Lloyd's seems to have won over most non-U.S. investors. A June poll by Market Opinion Research International for Lloyd's found in a sample of its members in Britain that 82% plan to

support the rescue package. What's more, Lloyd's, which takes three years to settle its books, is expected to announce on July 12 a record \$1.8 billion profit for 1993, the result of a rise in insurance rates following 1992's Hurricane Andrew. It will use some of the expected bonanza in premium income from 1993 to 1995 to fund its \$4.8 billion settlement offer. The rest of the money will come from names, agents, the sale of its headquarters building, its rapidly depleting reserve fund, and other sources.

All of this should help the plan clear its first hurdle o

INSURANCE

'LLOYD'S COULD COLLAPSE'

A revolt of its U.S. investors might thwart a rescue plan

It is the moment of truth for Lloyd's of London. Staggering beneath \$13 billion in losses accumulated between 1988 and 1992 and facing a tidal wave of lawsuits over alleged negligence and fraud, the world's oldest and most famous insurance market may not survive—at least not in its present form.

In coming weeks, Lloyd's "names," the 34,000 individuals worldwide who pledge their assets to back the exchange's policies, will decide whether to support the exchange's last-gasp \$4.8 billion rescue package. They're being offered a chance to end what has become for many a personal and financial nightmare in return for dropping their lawsuits against Lloyd's and agreeing to fund a new company to house Lloyd's past liabilities. The approval process begins on July 15. Most signs suggest that it will pass.

But there is a big wild card that could sink the deal: the 2,700 U.S. names, who are responsible for much of the ongoing litigation. So far, British regulators have barred Lloyd's from offering the settlement to U.S. names. Lloyd's and a team of state securities administrators

LLOYD'S BATTLE FOR SURVIVAL

1988-1989 The insurance market is hit by the Lockerbie and Exxon Valdez disasters, Hurricane Hugo, and the San Francisco earthquake.

1991 Lloyd's announces loss of \$790.5 million.

1992 Liabilities from decades-old pollution and asbestos policies mount. Names start suing.

1995 Lloyd's announces a rescue plan that includes \$4.34 billion to settle litigation and create a new reinsurance facility to handle pre-1993 claims.

1996 Settlement offer is raised to \$4.8 billion. Lloyd's faces Aug. 28 deadline to prove to British regulators it has enough capital to stay in business.

DATA: LLOYD'S OF LONDON, ULTIMATE RISK BY ADAM RAPHAEL, BUSINESS WEEK

July 15, when the roughly 17,000 names who were active in the years 1993 to 1995, including corporate investors, vote whether to contribute their \$682 million share of the settlement fund. "We're being offered more to settle than we're likely to receive from litigation," concludes Michael Deeny, chairman of the Gooda Walker litigation group, which plans to recommend on July 11 that its 3,094 members take the offer.

NIMBLE ENTREPRENEURS. Even if Lloyd's pushes through its rescue plan and satisfies British regulators that it is solvent, the market will look very different from the one that had its origins at Edward Lloyd's 17th century coffeehouse. Its unique capital structure—with individuals backing the market "down to their last cufflink"—is becoming a thing of the past. Indeed, for the first time, in 1994, Lloyd's allowed \$2.5 billion from corporate investors into the market. Corporate capital now accounts for 30% of Lloyd's \$15.5 billion in underwriting capacity base. With virtually no new names joining Lloyd's on an unlimited liability basis, most observers believe the market will be dominated by corporate capital by the turn of the decade.

This raises the question of whether Lloyd's will be able to retain its edge over traditional insurance companies in writing unusual, complex risks. Despite its recent crisis, Lloyd's has managed to maintain its share of the global reinsurance market in the face of threats from new centers such as Bermuda. But if it is to grow, Lloyd's will have to reinvent itself. To that end, it plans a broad internal review this fall that will examine its capital structure, regulation, and management.

In attempting to reform its market, Lloyd's runs the risk of losing what has been its great strength. Its investors have a "history of being entrepreneurial and more innovative than many insurance companies," says Andrew J. Campbell-Hart, managing director for insurance of S&P's Rating Services in Europe. But with names replaced by corporate investors and Lloyd's tradition of unlimited liability fading, it could lose its uniqueness and become just another insurer. "This represents a fundamental change," says Campbell-Hart.

Adds Adam Raphael, author of *Ultimate Risk: The Inside Story of the Lloyd's Catastrophe*, a Lloyd's member, and chairman of a litigating group: "The old Lloyd's is dead. The question now is whether a new Lloyd's can arise from its ashes." With the heavy burdens of its past, that will be no easy task.

By Julia Flynn in London, with Vanette Byrnes in Los Angeles and Sandra Dallas in Denver

BROKERAGE FIRMS

THIS VIRTUAL BROKER HAS REAL COMPETITION

E*Trade battles Charles Schwab, eBroker—and internal bugs

To some, the exploding world of electronic commerce is an exciting frontier. But to Christos M. Cotsakos, the animated chief executive of E*Trade Group Inc., it's also a war zone. "We're the infantry on the beach," says Cotsakos, whose brokerage service was first to stake a claim in online trading in 1992. It is now battling new competitors, fixing snafus, and preparing to be the first firm of its kind to go public. By being first, "you get blood on your spear, but you know the terrain better than anybody," he says.

War metaphors come easily to the decorated Vietnam veteran. After all, says Cotsakos, who has been on the job since March, "I know what it feels like to get your butt shot off." It may happen again, as more than 20 firms, including such stalwarts as Charles Schwab Corp. and Fidelity Investments, gun for a piece of the Internet's coveted financial marketplace. Already, rivals are eating away at the edge E*Trade has had on them—the once incomparable \$14.95 commission. So far, eBroker has beat that with \$12 trades,

and Schwab just reduced its fee \$10 to \$29.95 per trade.

That's not E*Trade's only hurdle. It also must justify the giddy price-earnings multiple it seeks as an Internet stock, rather than the more mundane multiple of a discount broker. Revenue—

\$23.3 million last year—has grown an average of 125% annually since 1991. Even so, the expected offering price of \$11 to \$13 a share would be 133 times earnings for the past 12 months. Schwab trades at a p-e of 24.

Yet Internet-crazed investors might still buy the IPO, which is scheduled for August. E*Trade has the largest volume of Internet trades—2,500 daily and does 75% of its trades online. While a mere 800,000 investors trade online now, that number is expected to grow to 1.3 million by 1998, and individuals could manage

\$30 billion in mutual-fund assets online by the year 2000, according to Forrester Research Inc. "It's going to be a huge market segment," says Paulette Donnelly, an analyst at Simba Information Inc. in Wilton, Conn. To cater to that market, E*Trade is launching an online investment bank that will sell individual investors shares in IPOs. "We'll work like traditional banks, except without a sales force or a road show," explains E*Trade's David M. Traversi.

LATE NOTICE. But E*Trade must convince investors to overlook its myriad problems. A computer hardware failure in May, for instance, left many customers unable to access their accounts for 2½ hours. That led to a \$1.7 million payout to clients who lost money in the market. And customers gripe nonstop about not being notified promptly when their trades are executed. "I had a stock for a week without know-

E*TRADE GROUP INC.

BUSINESS

Electronic brokerage service

HEADQUARTERS

Palo Alto, Calif.

EMPLOYEES

245

TOTAL ACCOUNTS

65,000

MONTHLY TRADING VOLUME

170 million shares

UPCOMING PUBLIC OFFERING

6.8 million shares

FILING RANGE

\$11-\$13

DATA: SEC FILING



CEO COTSAKOS: His online firm has scheduled a public offering for August

ing I had it," grumbles Holly Cahill of Manchester, N.H. Customers even considered suing E*Trade to recoup losses.

Behind the snafus was E*Trade's too-rapid growth, which it engineered through ubiquitous ads. In 1996's first five months, active accounts swelled from 38,000 to 65,000 and monthly trading volume tripled from 50 million to 170 million shares. "Everybody was

caught by surprise," says Cotsakos, who endured startup problems during his 19 years at Federal Express Corp. Starting in May, the company reduced its ads for six weeks to stem the huge expansion.

E*Trade has already upgraded its technology and beefed up its staff. In early July, it set up a remote backup system to increase capacity and take

over in the event of another computer breakdown. And E*Trade now clears its own trades, which lets it improve confirmation times. Telephone waits are down from more than 20 minutes to a still hefty five minutes. It's unclear whether these initiatives will keep E*Trade ahead of the advancing troops—a tall order even for a group of warriors.

By Linda Himmelstein in Palo Alto

MARKETS

WILL THE BULL HEAD NORTH?

Canadian stocks rally as exports and commodity prices rise

Lloyd Atkinson, chief investment officer at Toronto-based MTA Investment Counsel, is used to getting a quick brush-off from foreign investors. "Their view has been, why would anyone invest in Canadian stocks?" he says. No wonder: Compared with U.S. stocks, Canadian equities have looked tepid. For the five years ending June 30, the benchmark Toronto Stock Exchange Composite 300 Index has earned an average annual return of 10.8% vs. 15.7% for the Standard & Poor's 500-stock index. Last year, Canadian stocks logged less than half the U.S. market's gain.

But now, with the U.S. bull market slowing, Canada is suddenly looking far more attractive. Many Canadian strategists believe rising commodity prices and a dramatic improvement in Canada's economic fundamentals should power the TSE index to a 15% to 20% gain over the coming year, well above the single-digit advances they foresee for the S&P. Canadian stocks may look even better for U.S. investors if, as expected, the Canadian dollar strengthens.

SHRINKING DEFICIT. "The late stage [of an economic] cycle is when Canadian markets typically outperform the U.S.," notes George Vasic, chief strategist at Bunting Warburg Inc. That's when commodity prices are strongest. Metals, oil and gas, and other resource stocks make up about 40% of the TSE 300—over three times their weight in the S&P 500. The recent collapse in copper prices was largely the result of a trading scandal at Sumitomo Corp. "The outlook for natural resources is bullish," says Patricia M. Mohr, an economist at the Bank of

Nova Scotia. The Scotiabank Commodity Price Index, a measure of commodities exported from Canada, hit a record 131 in May, the latest date available, up 11.3% in a year.

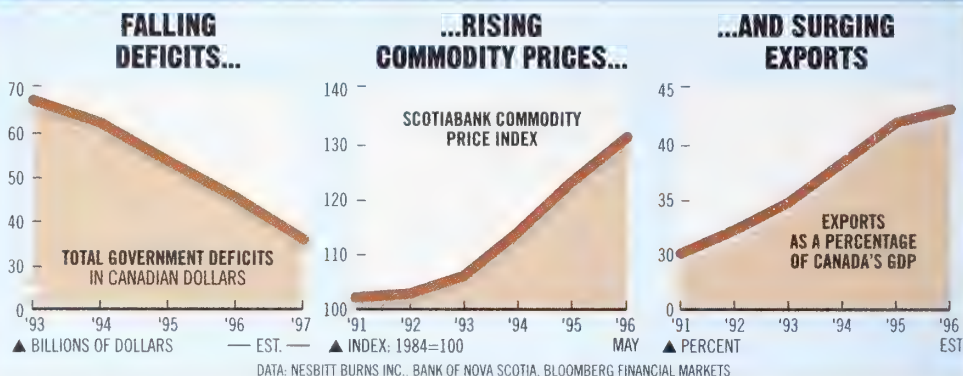
Improving economic fundamentals should also help Canadian stocks. Huge cuts in government spending are shrinking the budget deficit. That has allowed the Bank of Canada to bring short-term

more earnings growth in Canada over the next two to three years," says Vasic. The biggest winners, adds Diane Urquhart, manager of equity research at Scotia Capital Markets, will be the world-class resource and manufacturing companies responsible for the astonishing surge in Canadian exports, which now account for fully 40% of Canada's gross domestic product (chart).

Urquhart is especially bullish on nickel giants Inco Ltd. and Falconbridge Ltd., which benefit from rising prices. Stronger pulp prices should help such forest-product companies as Abitibi-Price, figures Josef Schachter, global strategist at Richardson Greenshields. And many are bullish on midsize oil and gas companies.

Toronto has long been a magnet for gold bugs. After soaring earlier in the year, gold stocks plunged 16% in June

The Case for Canadian Stocks



interest rates below those in the U.S. And inflation is just 1.5% a year.

Political waters are calmer, too. Last year, worries that Quebec separatists might win the independence referendum held the TSE to a 14.5% total return. Now, with another vote at least two years off, foreign investors are coming back at a near record pace. And Canadians are piling into mutual funds. Equity fund assets climbed to a record \$35 billion in May, up 33% this year. "There's a lot more firepower available," says Subodh Kumar, chief strategist at CIBC Wood Gundy Securities.

Moreover, partly because Canada's economic expansion has lagged behind the U.S.'s, "we expect substantially

The sell-off was punctuated by an abrupt reversal in the speculative frenzy surrounding so-called junior mining companies, which are exploring for gold and other minerals but typically have little actual production. Most analysts expect the larger gold companies to stage another rally.

Ironically, a far bigger threat to the TSE is Wall Street. A substantial correction in the U.S. market might rattle the Canadian market. But even if that happens, "any dip in Toronto would be less severe than the U.S.," predicts Kumar. With all the fundamentals pointing in the right direction, the message for investors is clear: Go north.

By William C. Symonds in Toronto

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EDITED BY AMY DUNKIN

JUST OVER THE HORIZON—SPACE-AGE CELLULARS

From the beginning, what many of us wanted was a phone we could carry with us. So desperate were we that we gladly welcomed the first cellular mobile phones, even if they seem in hindsight like the large portable

radios the Army used during World War II. But over the past few years, mobile phones have gotten smaller and lighter. Now there are models that fit into the palm of your hand. The lightest of this new wave, at 3.1 ounces, is the StarTac from Motorola. Its flip-up design will remind *Star Trek* aficionados of the communicator used by Captain Kirk.

The StarTac will give you up to 60 minutes of continuous talk time or 12 hours of standby time before it needs recharging. If you need more time to chat, a variety of extra-capacity batteries is available. The largest of these offers 210 minutes of continuous talk time or 41 hours of standby time, boosting the overall weight of the StarTac to 5.9 ounces. But what's cool about this phone is that it's small enough to carry like a pager. Or if you'd prefer, you can even wear it like a necklace: The \$1,500 price tag makes it something you'll want people to notice.

DICK TRACY. A lot less expensive at \$500 and only slightly heavier is Sony's CM-RX100 mobile phone. This palm-size device that resembles a miniature walkie-talkie feels a little dense because its 6.7 ounces are packed into such a small space. At first glance, you might wonder how to speak into it. Not to

worry: A small microphone swings out from the side of the body, so talking into the CM-RX100 is much like using a regular phone. Despite its small size, the CM-RX100 is

powerful, offering two hours of continuous talk time and 24

hours in the standby mode.

Small size and light weight are great, of course, but a mobile phone should offer more than just talk. When we think about the ultimate mobile phone, Dick Tracy's wristwatch-like voice-and-video-communication device comes to mind. The wristwatch part is a long way off, but by the end of the year you will be able to get a wireless device that can do almost as much. AT&T Corp.'s new 10-ounce Pocket-Net Phone, unveiled July 15, is a combination cellular phone and wireless data device that can send and receive both voice and data messages, even access the Internet, all for \$500. The phone is slated to be available to corporations by yearend and to con-

sumers in early 1997. Pocket-Net looks and feels like a cellular phone but has a small liquid-crystal-display screen on the top. You use the phone keypad to punch out messages. Voice calls are sent via standard cellular networks, while E-mail, faxes, and other data are sent over wireless networks enhanced with digital data transmission.

For even more functions, there's the Nokia 9000 Com-

municator. It's being introduced in Europe, but it should arrive in the U.S. by next year with an estimated price of \$2,000. At first blush, the Nokia 9000 looks like a regular mobile phone. But it splits open to reveal a small keyboard and screen, sort of like a handheld computer.

Both the AT&T and Nokia devices allow you to transmit and receive E-mail. Second

DREAM MACHINES

LEFT: NOKIA 9000

It works via a digital network (\$2,000)

MIDDLE: SONY

CM-RX100 This palm-size model packs a powerful punch (\$500)

RIGHT: MOTOROLA

STARTAC It's light—and offers 60 minutes of talk time (\$1,500)



you can send and receive short messages, much as an alphanumeric pager does now. You can communicate to a fax machine. And if that isn't enough data, you can also subscribe to services that will provide everything from stock quotes to sports scores. Nokia tosses in an electronic organizer with functions that include a calendar, address book, notepad, and calculator. No more carrying around a laptop computer simply because that's where all your phone numbers are stored.

The really exciting application, though, for both phones, is Internet access. Just imagine being able to dial up the Net from anywhere and being privy to all the data it can provide. True, the Nokia and AT&T screens

ON THE WAY The souped-up Nokia 9000 should arrive in the U.S. next year

are monochrome, so you won't get the rich graphics of the World Wide Web. But the way things work in the high-tech world, you can be pretty sure future models will feature a color screen that takes advantage of evolving video and data-compression technologies. What's more, you may eventually be able to listen to the Net as text-to-speech software is being developed.

NO HANDS. If all this information seems too much to deal with when you're on the phone, the Nokia 9000 connects to a computer, so you can download critical data. Downloading a file to a PC can be done using a serial cable or an infrared link. Files can also be sent directly to a printer via the infrared link. And while personal mobility is the Nokia 9000's strong suit, an adapter kit for hands-free use in a vehicle is also available.

So why can't most of us get one right now? The Nokia 9000 is designed to work with a digital mobile-phone network and will not operate on the current analog system used by cellular phones. A digital network, called a personal communications service (PCS), is slowly being rolled out in the U.S. But at present, service is available only in Washington, Honolulu, and Salt Lake City.

PCS may be the mobile-phone service of the near future, however. With PCS, you could have what industry insiders call a "fixed wireless" telephone. Instead of a wired telephone with one number

and a mobile phone with another, you would have a single PCS phone that would work at home or on the road. To make this one-person, one-number notion work, wireless phone calls would have to be priced competitively with wired calls, which isn't that far-fetched. The Scandinavian countries, in fact, are actively pursuing this goal.

The one-person, one-number idea isn't entirely foreign to the U.S., either. Chicago-

based United States Cellular is rolling out a new hybrid telephone called the Carry Phone, which is based on a similar premise. Carry Phone works like a cordless phone inside the house—the base station is connected to the wired network—but operates like a cellular phone once you leave. This phone effectively bridges the gap between wired and wireless networks, but it still leaves something to be desired: You must use two phone numbers. Carry Phone, which weighs less than a pound, is available in cities where United States Cellular operates. It leases for \$20 per month in addition to calling charges. Wired and wireless phone calls are billed separately so you can see where costs are incurred.

PRIVACY. Nevertheless, Carry Phone and other existing analog wireless systems don't offer the potential benefits of a digital mobile-phone system. PCS should lead to a proliferation of smaller, inexpensive handsets and less expensive service. PCS phones use smart cards containing microchips so subscriber information is not embedded in the phone, thereby reducing fraud and theft—since the phone won't work unless the owner inserts the card. Because of the numerous antennas the system uses, PCS also works within buildings and tunnels. You can even develop private networks that operate only in designated areas. And the antennas providing the link to the network are smaller and less obtrusive—they can even be disguised as trees. But until the PCS rollout is further along, the Nokia 9000 will remain just a dream. The AT&T phone, too, is still a way's off. For now, palm-size talk-only models you can display around your neck or on your belt are the status symbol of mobile phones. *Frank Vizard*

The Must-Have Mobile Phone

Personal communications service (PCS) cellular telephones are slowly rolling out across the U.S. Since PCS is a digital system, it offers advantages over the existing analog advanced mobile-phone system (AMPS). The top 10 reasons why a PCS phone is a major advancement:

- It communicates voice and data simultaneously
- You can be assigned one number, no matter what your location
- Transmission times are faster
- It provides Internet access
- Handsets are lighter
- Batteries last longer
- It's less expensive to use over the long term
- The network antenna is smaller and less obtrusive
- It operates within buildings
- Stock quotes and other data subscription services are available

DATA: BUSINESS WEEK



NOW, THAT'S A HOME THEATER

You've nuked the popcorn, dimmed the lights, and packed your den with friends who share your passion for movies. Just before showtime, you slip what appears to be an ordinary five-inch compact disk into a slim black box that resembles a CD player or VCR. Someone presses a remote control and an explosive soundtrack grips the room. An instant later, your guests are having a close encounter on the big-screen TV with Arnold, Clint, or the Caped Crusader.

That was no ordinary compact disk, all right. It was a digital videodisk (sometimes called digital versatile disk), or DVD, a new format that backers say will enable consumers to watch movies at home as they were meant to be seen. DVD players will start at about \$500, though legal and technical hurdles might delay their arrival until next year.

MULTILINGUAL. The first thing you'll notice about DVD is a bang-up digital soundtrack. Then there's a supersharp color picture that comes pretty darn close to a studio's master copy. In technical terms, a DVD can display up to 720 pixels per horizontal line vs. 320 for a standard VHS, though you'll need a high-end TV that can take advantage of the difference. A single-sided, single-layer DVD platter can contain 4.7 gigabytes of data, or more than the capacity of seven audio CDs or over 3,000 floppy disks. (And using both sides of the disk, developers can stuff in even more data.) That translates into about 133 minutes of video, which would cover roughly 95% of all new film releases.

What's more, the studios have the capability to load up to eight different audio lan-

guage tracks and 32 subtitle tracks on one DVD. Hollywood can also record alternative versions of the same film on one disk, so parents might watch an "R" cut while using passwords to let the kids only take in an edited-down PG-13 version. The disks can display "multiple aspect ratios": The 4:3 or "pan and scan" ratio, which may chop off a third of the movie's picture on a standard TV, or the

movie. A Clint Eastwood DVD might let fans call up a filmography of his acting and directing credits, clips cut from the theatrical release, or other behind-the-scenes footage. Such versions have been done for laserdiscs.

For all its promise as a video playback machine, DVD probably has greater potential as a replacement for CD-ROMs.

A DVD-ROM disk not only takes advantage of DVD's vast storage capabilities but is much faster than most current CD-ROM drives. And people will be able to watch full-screen movies on their personal computers.



wide-screen, 16:9 "letterbox" ratio that duplicates the image in a theater. The disks might also hold movie scenes from multiple camera angles. As with CDs, consumers can get quick access to any part of the disks, which might cost as little as \$20.

Where DVD gets more intriguing for film fanatics is in the kind of content that could eventually accompany a

A number of software developers are working on reference and entertainment DVD-ROM titles. Digital Directory Assistance in Bethesda, Md., has already released a DVD-ROM disk of its PhoneDisc PowerFinder, which contains 112 million telephone listings. The CD-ROM version of PowerFinder takes up six disks. Similarly, Tsunami Media claims its up-

coming *Silent Steel* interactive movie will use a single DVD-ROM disk vs. four CD-ROMs. Tsunami CEO Ed Heinbockel expects the price of DVD-ROMs to be about the same as conventional CD-ROMs. Anyone who has already invested heavily in CD-ROMs can breathe a sigh of relief: DVD-ROM players will

DREAM MACHINES

be able to handle CD-ROM software.

So how soon will DVD come to a home theater or PC near you? The movie studios, the PC industry, and consumer-electronics manufacturers are still grappling over technical and legal issues to prevent illicit copying of these digital disks, hurdles that might delay the DVD rollout until 1997. But such avid DVD backers as Toshiba, Panasonic, and Thomson Consumer Electronics are sticking to the fall 1996 time frame for a launch. "I believe we are very close," insists Craig Eggers, director of DVD marketing at Toshiba America Consumer Products.

The companies have already demonstrated impressive working DVD models. Thomson's RCA base DVD player will start at \$499. A model with a universal remote and other features will cost \$100 more. Toshiba has announced two models with suggested

AN RCA DVD PLAYER
The digital videodisk launch could come by '97

retail prices of \$599 and \$699. At the PC Expo trade show in New York in June, Panasonic and Toshiba displayed DVD-ROM units. Panasonic plans to market the drive in DVD upgrade kit that might cost \$500 to \$700.

With all of the industry muscle behind DVD, it is only a matter of time before consumers get to render their own verdict on the new format. Their final thumbs up or thumbs down will determine whether or not DVD has one of those glorious Hollywood endings—or is a Tinseltown dud of extremely large proportions. *Edward Ba*

High-quality pic and sound and pluses for film fanatics

THE CAMCORDER COMES OF AGE

Most people buy camcorders to create vacation travelogues or capture the wonder years of their children. To them, the under-\$1,000 8mm and VHS-format analog camcorders produce perfectly acceptable videos of their camel ride by the Pyramids or little Jamie's first birthday party. But the most dedicated hobbyists, or anyone who uses a camcorder for business, demand more: smashing videos that have a commercial feel.

Videophiles may be getting their wish, though they'll have to splurge to make the dream come true. A handful of camcorders conform to yet another new format that exploits the digital universe of ones and zeros, the aptly named DV, or digital video. Recent arrivals from JVC, Thomson (RCA), and Sharp join DV models from Panasonic and Sony. The camcorders start at around \$2,500 and go well beyond four grand—a considerable premium over Hi 8 and Super VHS machines, the previous gold standard for consumer camcorders.

DV machines deliver pristine, "noise-free" images with less jitter than is apparent with analog videos, plus the ability to enhance the pictures with special effects. They also provide excellent CD-quality sound. **"HUGE STEP."** The camcorders generally produce videos with about 600 horizontal lines of resolution, compared with about 400 lines for Hi-8 and Super-VHS and just 240 lines for standard VHS or 8mm. "The progression from analog video to digital video is a huge step forward," says Lancelot Braith-



are recorded onto a minicassette that's about one-twelfth the size of a VHS tape. To watch on a big screen, you connect cables from the camera to your TV or VCR. At around \$13 and \$20 for 30-minute and one-hour versions, blank DV tapes cost more than other formats and are shorter in length.

Folks can use the camcorders to edit and dub recorded scenes onto an ordinary videotape with minimal degradation of picture and sound quality. At present, however, only the Sony DCR-VX1000 and

POCKET PAL

JVC's GR-DV1 is small and light—and lets you play with a variety of special effects

waite, technical editor for *Video Magazine*. All the digital machines generate superb images. But the Panasonic and Sony are the most expensive models. Sony and Sharp have three, rather than one, charge-coupled devices, or CCDs—chips used to record the images. So they render the most accurate color pictures. Videos

DCR-VX700 permit digital output that adheres to the IEEE 1394 standard, which allows multiple copies indistinguishable from the original. To do that, you'll need to connect one Sony digital camcorder to another (or to a 1394-compliant computer). Others are awaiting the outcome of copyright negotiations among Hollywood, the PC industry,

and consumer-electronics companies—the same holdup that has delayed the launch of digital videodisks.

Consumers can take advantage of DV's snapshot mode, which effectively turns digital camcorders into high-quality digital still cameras. On Panasonic's PV-DV1000, for example, users can record up to 290 still pictures on a 30-minute tape or 580 on a one-hour tape. The images can be accompanied by seven seconds of sound. Hard copies can be produced by connecting the camera to a printer. "If you need to capture a lot of images, a digital camcorder is the best way to go rather than a digital still camera," says Michael McNamara, technology editor for *Popular Photography*.

FADES AND WIPE. I tried out JVC's GR-DV1, a little dynamo that weighs just over a pound (with battery) and can fit into a trouser pocket. It's a twin to the RCA CC900D. The camcorder can be inserted into a docking station, which you can leave attached to a TV set or VCR, thereby eliminating the need to replug cables every time you want to watch a video. The JVC lets you add a variety of special effects: strobe (a series of consecutive snapshots), sepia (scenes with a brownish tint reminiscent of old photos), and echo (ghosts that lend a fantasy feeling). You can also play around with fade, wipe, and dissolve ef-

fects to jump from one scene to another. Even better, you can add these effects later.

Sharp's VL-D5000U ViewCam is the most expensive of the DV lot. But it boasts a terrific 5-inch LCD viewfinder (in lieu of the traditional viewfinder), the largest around. As with other Sharp ViewCams, the lens rotates a full 270 degrees, which makes it a cinch to record yourself in a video. Better check your hair: A digital video shot will be all too true. *Edward Baig*

DREAM MACHINES

The New Digital Stars

MODEL/PRICE	COMMENTS
JVC GR-DV1/\$3,000 RCA CC900D/\$2,599	The smallest and lightest models, these near-twins fit in a pocket. They include a docking station that lets you leave cables attached to a TV or VCR.
PANASONIC PV-DV1000/\$4,200	Turbo-zoom feature lets you zip from tight to wide angle or vice versa in less than two seconds.
SHARP VL-D5000U/\$4,596 SHARP VL-DC1U/\$3,595	Feature 5-inch and 4-inch LCD monitors, respectively. Users can shoot from almost any angle while watching the scene on the LCD screen.
SONY DCR-VX1000/\$4,199 SONY DCR-VX700/\$2,999	Only models adhering to the "1394" standard, so you can make a copy identical to the original.

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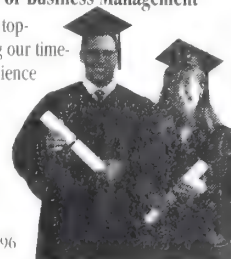
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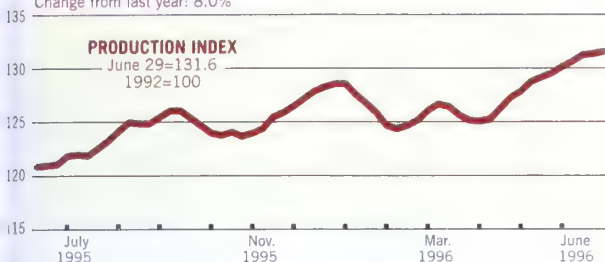
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Business Week Index

PRODUCTION INDEX

Change from last week: 0.2%
Change from last year: 8.0%



The index is a 4-week moving average.
The production index increased during the week ended June 29. Before calculation of the four-week moving average, the index rose solidly, to 132.2, from a revised 130.8 in the previous week. Seasonally adjusted rail-freight traffic and truck production were particularly strong. For the entire month of June, the index increased to 131.6, from a reading of 130 in May.
The leading index will be unavailable for an indefinite period of time.

3W production index copyright 1996 by The McGraw-Hill Companies.

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (7/5) S&P 500	657.44	670.63	19.3
CORPORATE BOND YIELD, Aaa (7/5)	7.79%	7.83%	5.1
INDUSTRIAL MATERIALS PRICES (7/5)	105.6	105.8	-8.2
BUSINESS FAILURES (6/28)	NA	NA	NA
REAL ESTATE LOANS (6/26) billions	\$508.2	\$508.7	6.8
MONEY SUPPLY, M2 (6/24) billions	NA	NA	NA
INITIAL CLAIMS, UNEMPLOYMENT (6/22) thous.	355	357	-3.8

Sources: Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (7/9)	5.14%	7.80%	5.81%
COMMERCIAL PAPER (7/10) 3-month	5.54	5.50	5.73
CERTIFICATES OF DEPOSIT (7/10) 3-month	5.55	5.45	5.73
FIXED MORTGAGE (7/5) 30-year	8.36	8.49	7.86
ADJUSTABLE MORTGAGE (7/5) one-year	6.07	6.11	5.86
PRIME (7/9)	8.25	8.25	8.79

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

BUSINESS INVENTORIES

Monday, July 15, 10 a.m. edt ► Inventories led by manufacturers, wholesalers, and retailers likely edged up by 0.1% in May, as the median forecast of economists surveyed by MMS International, one of The McGraw-Hill Companies. Business inventories may have declined, however, because retailers and wholesalers have already reported declines in their May stock levels. Retail inventories rose 0.4% in April.

CONSUMER PRICE INDEX

Tuesday, July 16, 8:30 a.m. edt ► Consumer prices probably rose 0.2% in June, after May's 0.3% gain. Higher tobacco prices contributed to the increase. Exclud-

ing food and energy, prices likely rose 0.2% in June, the same small increase as in May.

INDUSTRIAL PRODUCTION

Tuesday, July 16, 9:15 a.m. edt ► Industrial output probably increased 0.4% in June, on top of a 0.7% jump in May, says the MMS survey. That's suggested by the increase in the factory workweek. The average operating rate for all industry likely rose to 83.3% in June from 83.2%.

HOUSING STARTS

Wednesday, July 17, 8:30 a.m. edt ► Housing starts in June probably stood at an annual rate of 1.45 million, up from a 1.43 million pace in May. Housing demand

remains strong despite the one-percentage-point rise in fixed mortgage rates.

INTERNATIONAL TRADE

Thursday, July 18, 8:30 a.m. edt ► The foreign trade deficit of goods and services likely narrowed to \$8.1 billion in May, from \$8.6 billion in April. After rising 1% in April, exports were probably flat, while imports, up 1.7%, likely fell slightly in May.

HUMPHREY-HAWKINS TESTIMONY

Thursday, July 18 ► Federal Reserve Chairman Alan Greenspan will testify on future monetary policy and the current state of the economy before the Senate Banking Committee.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (7/6) thous. of net tons	2,005	1,986#	4.9
AUTOS (7/6) units	10,160	133,605r#	-21.5
TRUCKS (7/6) units	10,199	112,871r#	-39.6
ELECTRIC POWER (7/6) millions of kilowatt-hrs.	69,553	70,734#	9.1
CRUDE-OIL REFINING (7/6) thous. of bbl./day	14,160	14.3/5#	-1.7
COAL (6/29) thous. of net tons	17,815#	18,470	-4.1
PAPERBOARD (6/29) thous. of tons	903.3#	890.0r	-5.2
PAPER (6/29) thous. of tons	823.0#	821.0r	-2.3
LUMBER (6/29) millions of ft.	474.0#	471.9	15.2
RAIL FREIGHT (6/29) billions of ton-miles	24.3#	24.6	3.8

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA1, SFPA2, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (7/10) \$/troy oz.	383.000	381.950	-0.6
STEEL SCRAP (7/9) #1 heavy, \$/ton	133.50	138.50	-5.0
COPPER (7/6) ¢/lb.	92.5	99.3	-34.6
ALUMINUM (7/6) ¢/lb	69.5	70.0	-18.2
COTTON (7/6) strict low middling 1-1/16 in., ¢/lb	76.43	77.64	-24.0
OIL (7/9) \$/bbl.	21.30	20.91	23.5

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (7/10)	110.08	110.13	87.48
GERMAN MARK (7/10)	1.52	1.53	1.39
BRITISH POUND (7/10)	1.55	1.56	1.60
FRENCH FRANC (7/10)	5.16	5.16	4.85
ITALIAN LIRA (7/10)	1534.3	1535.5	1610.8
CANADIAN DOLLAR (7/10)	1.37	1.36	1.36
MEXICAN PESO (7/10)	7.611	7.583	6.020

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

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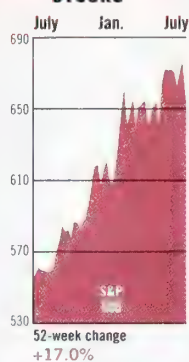
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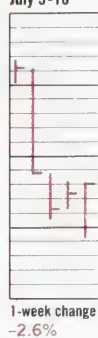
COMMENTARY

Stocks took it on the chin as a longer-than-expected employment report issued on July 5 sent interest rates soaring. While both bonds and stocks recovered somewhat by midweek, the damage was nonetheless extensive. The yield on the 30-year Treasury jumped 15 basis points in a week before, and the Dow Industrials and the S&P 500 index declined 1.8% and 2.5%, respectively. But as technology stocks continued to be pounded, the real damage showed up in the high-tech-heavy Nasdaq composite index, which fell a huge 3.5% for the week.

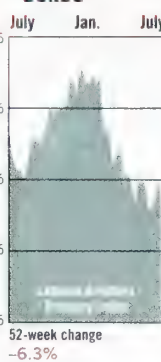
STOCKS



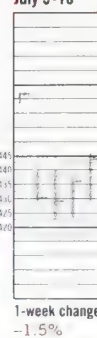
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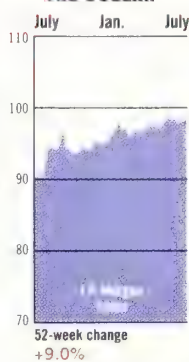
BONDS



July 3-10



THE DOLLAR



July 2-10



MARKET ANALYSIS

5. STOCKS

	Latest	% change Week	% change 52-week
DOW JONES INDUSTRIALS	5603.7	-2.0	18.5
NYSE COMPOSITE (S&P MidCap Index)	229.0	-3.4	11.6
NASDAQ COMPANIES (Russell 2000)	332.7	-4.1	13.3
DOW JONES COMPANIES (Russell 3000)	372.8	-3.0	16.4

FOREIGN STOCKS

	Latest	% change (local currency) Week	% change (local currency) 52-week
FTSE 100 (FINANCIAL TIMES 100)	3765.8	1.1	9.1
NIKKEI INDEX (NIKKEI INDEX)	21,778.9	-2.5	31.2
TSE COMPOSITE (TORONTO TSE COMPOSITE)	5098.3	0.7	8.2

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.27%	5.30%	5.53%
30-YEAR TREASURY BOND YIELD	7.08%	6.93%	6.55%
S&P 500 DIVIDEND YIELD	2.19%	2.13%	2.39%
S&P 500 PRICE/EARNINGS RATIO	18.9	19.4	17.2

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day moving average	664.6	668.1 r	Negative
Stocks above 200-day moving average	56.0%	63.0% r	Neutral
Speculative sentiment: Put/call ratio	0.69	0.59 r	Neutral
Insider sentiment: Vickers sell/buy ratio	2.57	2.52	Negative

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

1-MONTH LEADERS

	% change 1-month	% change 12-month
OIL EXPLORATION AND PRODUCTION	9.1	17.4
OIL WELL EQUIPMENT AND SERVICES	5.3	40.1
NATURAL GAS	5.1	31.9
SHOES	3.4	90.3
DOMESTIC OIL	2.4	13.2

Strongest stock in group

	% change 1-month	% change 12-month	Price
BURLINGTON RESOURCES	12.3	14.9	44 ³ / ₈
BAKER HUGHES	10.0	65.3	34 ¹ / ₂
CONSOLIDATED NATURAL GAS	14.8	46.6	54 ¹ / ₄
REEBOK INTERNATIONAL	7.1	-4.6	33 ³ / ₄
LOUISIANA LAND	11.7	48.0	58 ⁵ / ₈

1-MONTH LAGGARDS

	% change 1-month	% change 12-month
TRUCKING	-23.6	-37.2
AUTOMOBILES	-12.6	-1.3
COMPUTER SYSTEMS	-11.1	-1.5
TOYS	-11.0	16.6
HEALTH CARE SERVICES	-11.0	26.7

Weakest stock in group

	% change 1-month	% change 12-month	Price
CALIBER SYSTEM	-36.1	-43.2	23 ¹ / ₂
CHRYSLER	-15.9	14.7	56 ³ / ₄
APPLE COMPUTER	-22.1	-60.9	19
MATTEL	-11.8	16.3	25 ¹ / ₈
AMGEN	-11.1	32.7	53

MUTUAL FUNDS

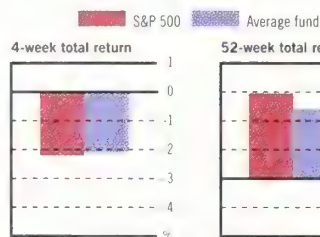
MORNINGSTAR INC.

LEADERS

	4-week total return	%
FONTABEL EASTERN EUROPEAN EQUITY	9.6	
WARBURG PINCUS JAPAN OTC COMM.	6.3	
MORGAN STANLEY INSTL. LATIN AMERICAN A	5.7	
	52-week total return	%
TURNER SMALL CAP EQUITY	66.4	
FRANKLIN GLOBAL HEALTH CARE	60.9	
PREMONT U.S. MICRO-CAP	59.6	

LAGGARDS

	4-week total return	%
STEADMAN TECHNOLOGY GROWTH	-16.9	
STEADMAN AMERICAN INDUSTRY	-15.9	
PREMIER STRATEGIC GROWTH A	-14.8	
	52-week total return	%
STEADMAN TECHNOLOGY GROWTH	-31.0	
STEADMAN AMERICAN INDUSTRY	-25.0	
STEADMAN INVESTMENT	-19.2	



RELATIVE PORTFOLIOS

DRUMCRAW-HILL

Dollar amounts represent the present value of \$10,000 invested one year ago in each portfolio

Percentages indicate 1-day total returns



U.S. stocks
\$11,949
-3.13%



Foreign stocks
\$11,138
-1.95%



Money market fund
\$10,531
+0.11%



Gold
\$10,184
+0.24%



Treasury bonds
\$9,766
-2.47%

Data on this page are as of market close Wednesday, July 10, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as

of market close July 9. Mutual fund returns are as of July 5. Relative portfolios are valued as of July 9. A more detailed explanation of this page is available on request. r=revised

WHAT WAGE-PRICE SPIRAL?

For some time, BUSINESS WEEK has taken a strong pro-growth position. We believe that U.S. productivity is higher than government statistics indicate and inflation is significantly lower. We see the global economy as severely restraining the pricing power of companies which recognize that in the current competitive reality they must generate profit by boosting efficiencies, not prices. In other words, we believe the U.S. can achieve growth rates higher than 2% without renewed inflation.

That is why the panicky reaction on Wall Street to the recent rise in wages is disquieting. News that, for the second quarter, hourly pay rose 3.4% from a year ago and the unemployment rate fell to 5.3% in June has led to fears of a new wage-price spiral and demands for the Federal Reserve to immediately hike interest rates (page 31).

We politely disagree. In fact, unlike Wall Street's inflation Cassandras, we celebrate what seems to be the end of two decades of stagnation in real wages. We're betting that hard-nosed CEOs are right when they say they can't raise prices. We're guessing they will absorb the cost of higher wages by cutting costs and boosting productivity, as they have done for the past five years. We think the U.S. can have high growth and low inflation, healthy profits and good wage gains. Our advice to the worrywarts: Think 1960s, not 1970s.

Everyone is finally getting a share of the gains. In this tight labor market, wages are going up for minimally skilled people, highly skilled employees, and even middle managers. Bureau of Labor Statistics data shows that the percentage of workers making the minimum wage of \$4.25 fell to 5.3% in 1995, from 6.6% in 1993. As for skilled workers, big companies are bidding them away from smaller companies, which are offering more training and pay. Middle managers still are getting downsized, but now 90% earn the same salary or better in new jobs. This is good for the economy and for society.

But what about wage inflation? Aren't higher wages threatening to push up prices everywhere? Hardly, thanks to global competition and higher productivity. Even industries with tight job markets are showing virtually no price increases. Take retailing, health care, construction, software, and aerospace. While McDonald's Corp. now pays new workers an average of \$5.30 an hour, Big Macs still cost the same as they did a year ago. Price inflation at restaurants fell to 2.7% in May. Medical services inflation is falling too, to 3.9% in May from 10% in 1991. New housing prices are up, but that's due to strong demand. Lumber and other construction material costs are down. Computer prices are falling. Global competition with Airbus Industrie is keeping Boeing Co. in check.

We can't resist throwing in a few other stats. Price inflation for new cars is running at only 1.5%, down from 8% in 1991, and there is zero inflation for used cars, compared with 16% in 1995. Woman's apparel had zero inflation in May, and even the rate of increase for tuition costs is at a record low of 2.6%. Remember when they were rising at 10% in 1992?

The truth is, even if you accept government inflation numbers at face value, there are few signs of faster inflation due to rising wages or anything else. Most key commodity prices are tame, and gold is off its highs. And unit labor costs remain low despite higher wages, thanks to higher productivity and declining growth in benefits payments. At a time when the growth rate for wages has jumped, the growth rate for employee benefits has dropped to 2.3%, from 3% last year.

If there were signs of a return of the dreaded wage-price spiral of the 1970s, the Fed would be right in leaning against the wind and raising rates to curb growth. But there aren't any. Just a few years ago, the Fed was convinced that an unemployment rate of 6% was inflationary. It wasn't. A rate of 5.3% probably isn't either. Fast economic growth is raising both profits and wages. We repeat: Growth is good.

CRONY CAPITALISM TAKES ITS TOLL

Call it *quanxi* capitalism, crony capitalism, or just the old boy network, but U.S. corporations are discovering that doing business in Asia increasingly requires a major rethink of classical market economics. Who you know often overshadows what you sell, and personal connections can matter far more than price or quality. It's hard to tell what "corruption" means. It's harder still to apply the free trade rules of the OECD and the WTO. But try we must.

Take China, where state-owned economic assets are now passing into the private sector. China's soaring economy is based on relationships between overseas Chinese and Western companies and local mayors, commune managers, and People's Liberation Army officers who control once-public property. Payments at the local level are part of doing business.

In such countries as Thailand and Indonesia, military and political groups control access to markets and require cash payments, "royalties," and other forms of money transfer for permission to invest. In Japan and Korea, crony capitalism takes the form of giant, interconnected corporations allied with government ministries. U.S. companies are trying to deal with Japanese *keiretsu* by joining them. Elsewhere in Asia, they use middlemen to gain entry and create joint ventures with local government officials, military commanders or party hacks.

But it is tough going. Crony capitalism puts U.S. companies at a competitive disadvantage. It is time for Washington to insist that those nations who enjoy the fruits of the open free trading system also play by its rules.



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ON BLACK: THE STREET'S DR. NOT SWEAT SHOP BACKLASH

NESS WEEK

July 29

BusinessWeek

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JITTERS!

With investors worried about earnings and interest rates, the long-awaited stock market sell-off finally hit.

Is that so bad? PAGE 24



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**"A pilot has to believe in his equipment.
That's why I wear a Rolex."** *Chuck Yeager*

Throughout his remarkable career, Chuck Yeager has shown an uncanny talent for what pilots call "pushing the edge of the envelope."

At 21, only three years after first boarding a plane, Yeager was leading a squadron of fighter pilots in World War II. And at the age of 24, he became the first person to fly faster than the speed of sound.

Yeager remains a man on the move. "I don't jump off 15-foot fences anymore," says Yeager, "but I can still pull 8 or 9 G's in a high-performance aircraft."

In all his exploits, Yeager depends on a rugged and reliable timepiece. "I wore a Rolex more than 40 years ago when I broke the sound barrier and I still do today," says Yeager.



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BusinessWeek

JULY 29, 1996

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JITTERS!

Is there a bear at the door? Probably not. Odds are that the scary Wall Street sell-off is a healthy correction

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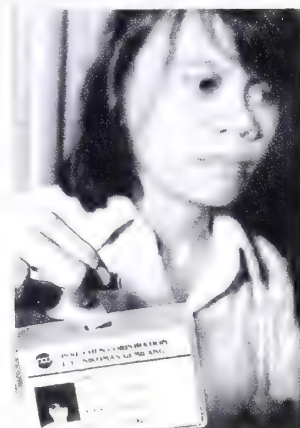
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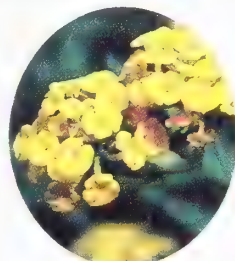
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EDITED BY LARRY LIGHT

STRANGE BEDFELLOWS

THE TOMATOES OF WRATH

U.S. AMBASSADOR TO Mexico James Jones has gotten involved in a trade dispute over Florida growers' complaints about cheap imported Mexican tomatoes. But it raises questions about whether he's too close to Mexican interests.

In June, during a federal probe of surges in tomato imports, Jones met with a group of Mexican tomato producers on the issue. An embassy aide's handwritten memo says Jones "expressed support" and asked that the



MEXICO: The offending crop

growers' Washington law firm "contact him directly with ideas they have for him so that he could help."

Jones confirms he then met with the growers' lawyer, Robert Herzstein of Shearman & Sterling, in Washington. But he insists it was

TALK SHOW "That which tends to bring the government into hatred or contempt, or which excites disaffection against the government." —Singapore's definition of material it won't allow Internet providers there to generate

only about getting U.S. and Mexican growers to negotiate. Herzstein says the two were "just comparing notes." On July 2, the U.S. International Trade Commission ruled that Mexican tomatoes weren't seriously harming U.S. suppliers.

While not illegal, Jones's meeting with the lawyer about a case before the ITC has provoked concern in Washington trade circles. "It doesn't help the image of an independent, quasi-judicial" ITC, says former ITC Chair Paula Stern. Jones, noting that he never approached the ITC on this, says he has kept the Administration and Congress informed of his actions. *Amy Borrus*

OLYMPICS '96

INVASION OF THE TCHOTCHKE SELLERS

ATLANTA IS OVERRUN WITH street vendors hawking games goodies, gripes the International Olympic Committee. The IOC says this makes the Olympics look too much like a flea market. Plus, it says, the T-shirts and knickknacks these 4,500 merchants are selling could eat into the gift biz at pavilions of corporate sponsors (who paid up to \$40 million to be there).

The IOC, which has complained to the city about licensing too many people, vows to require future Olympic

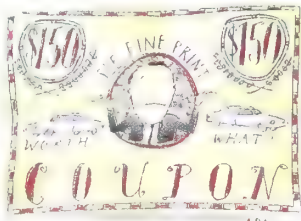


sites to keep local vendors to a minimum. At the '84 Olympics in L.A., there were very few, says the IOC. But Atlanta, which stands to collect some \$3 million from licensees, says the vendors (80% of them minorities) should be able to benefit from the games, too. *Nicole Harris*

RETAIL TALES

LET THE PUNISHMENT REWARD THE CRIME

IS THIS A GOOD deal? Toyota, accused of overcharging some 3 million customers by \$20 to \$400 per car, wants to make amends by offering each of them a coupon worth \$150. They can use it toward a purchase or lease of a new Toyota (average price: \$18,600) or for repairs on their old one. That's the settlement the auto maker has



reached with attorneys in a class action, pending a judge's O.K.

Dismayed by a rash of similar settlements (airlines, General

Mills, General Motors), critics label coupon payoffs a ripoff. Columbia University law professor John Coffee says few customers take advantage of a coupon because it's usually just a fraction of

an item's price. Court-appointed experts figure purchase redemptions for Toyota will range from 13% to 36%.

Another knock on coupons is that they're a boost for the wrongdoers since they force people to buy something. Recipients would be allowed to sell the coupons to others.

The Toyota suit charges that from 1990 to 1994, some dealers wrongly added ad dollars to dealers' costs, but the money was never spent. Toyota says it did nothing wrong and is settling to avoid court expenses. Certainly, one group will benefit: Plaintiffs' lawyers will get \$4.2 million in fees. *Lisa Sanders*

WHEELER-DEALERS

PLAYING THE OPTIONS SHUFFLE

HERE'S AN INTERESTING coincidence. In February, ADT Chairman Michael Ashcroft traded 3 million in-the-money company options for 8 million new options at a higher strike price. If he had cashed out his old options instead, he would have bagged at least a \$7.2 million profit.

Turns out that the new options became even more valuable. Come early July, Wayne Huizenga's Republic Industries agreed to buy alarm-system provider ADT. The all-stock deal initially valued ADT at nearly \$5 billion, or \$26 a share. If Ashcroft, whose new options would fully vest upon a change of control at the company, could sell



ASHCROFT: Shrewd move?

at that price, he would net \$80 million. ADT and Ashcroft didn't return calls seeking comment on whether he had any idea back in February that ADT might be sold. Republic also wouldn't specify when the deal was first discussed but says it was put together fast. ADT's board has been generous to Ashcroft in other ways, paying him \$5.2

million and granting him 1.5 million options in 1995—even though net income fell 50%.

Sadly for Ashcroft, his chances of making a killing have dwindled. While ADT hit 24% the day of the Republic announcement, the market sell-off and uncertainty about the deal's prospects have dropped the stock to around 18%. Below that, he would not come out ahead from the swap. The stock closed at 19 on July 17. *Mark Maremont*

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SLUGFESTS

CONDUCT CODE? MAYBE NOT

FINANCIAL PLANNERS ARE battling one another over a proposed conduct code, which opponents say will only provide ammo for client lawsuits. An existing ethics statement forbids the nation's 32,000 Certified Financial Planners from cheating their clients. The CFP board, which

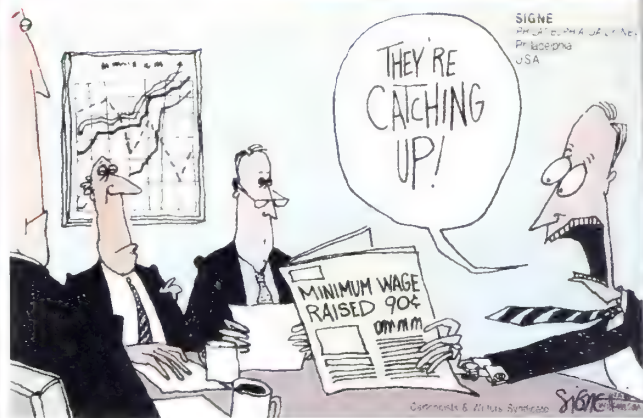
certifies planners, is looking at going beyond that to a list of things every CFP must do, such as assessing clients' investment goals and gauging their risk tolerance.

Backers of the code, called

the Practice Standards, figure that it would be a good way to build public confidence in CFPs. Says Kevin

Condon, chairman of the Maryland CFP society: "We must pay this price to get the charlatan with the yellow pad out." Last year, only 36 planners got stripped of their certifications, usually after client complaints.

A tougher code also could stave off government regulation, which several congressional bills threaten to impose. The threat hasn't yet galvanized the CFP board to



PRODUCT PEEK

THE BELLE OF THE GOLF BALLS

THEY'RE FLYING OFF THE shelves as fast as they are off the tee. At \$3 each, Top Flite's new Strata balls which appeared in June, cost



\$3 APIECE: But sales are brisk.

three times as much as regular golf balls. Still, pro shops are hard put to keep them in stock.

Spalding-owned Top-Flite hopes the Strata's popularity will boost the company's No.2 market share in high-end balls from 20% to 30% by next summer, overtaking leader Titleist. Used by pros and low-handicap golfers, the hardy balls are one-third of the \$602 million golf-ball market, where Top-Flite dominates overall. Titleist, contending its ball is best, says it isn't worried by the Strata.

The Strata's patented three-layer construction has won raves from serious golfers because, they say, it has dual qualities that are seldom found in a single ball: It both handles well on the green, and most important, it soars far on the fairway. Farther, Top-Flite says, than other balls. *Jennifer Merritt*

AFTERLIVES

A FAREWELL TO THE RAT RACE

YOU KNOW the hard-driving executive who "retires" with a sack of cash and quickly grows restless. In short order, he's heading

lion. "But I'm very satisfied with my lot in life."

Wolf flunked his retirement. Within months, he joined Air France as a high-level consultant. Last January, Wolf signed on as CEO of troubled USAir. Wolf, now 54, has reassembled part of his top

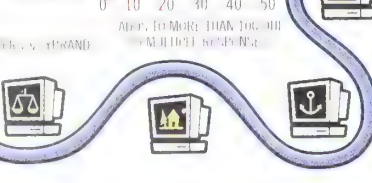
team from United, but Pope wasn't interested.

Pope hasn't given up all of his business interests. He is busy managing his money. And he's a board member at auto-parts maker Federal-Mogul and at MK Rail, the troubled railcar manufacturer controlled by Morrison Knudsen. He's also treasurer of Chicago's respected Shedd Aquarium. *Susan Chandler*

THE BIG PICTURE

UNTANGLING THE WEB

Where do people find out about Web sites? With 90,000 to choose from, a lot use good old-fashioned word of mouth. Traditional, supposedly antiquated media are another rich source.



another company.

Not Jack Pope. The former United Air Lines president and chief financial officer is having a blast—reading all of Ernest Hemingway and John Steinbeck and giving daily piano lessons to his three children. Plus, he's traveling with his family—to Italy, China, and Australia.

When Pope and then-Chairman Stephen Wolf left the airline in July, 1994, as part of a \$5 billion employee buyout both said they would stay home. "Most people thought I mentally couldn't do it," says Pope, 47, who walked away with more than \$10 mil-

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A WEALTH
OF ECONOMIC OPINION

I read your Cover Story ("Economic growth: A proposal," July 8) with interest, and I agree with your broad points. Regarding taxes, however, I believe that we have huge amounts of savings locked up in capital gains that could be released to invest anew with a simple tax fix: index capital gains to inflation. A surprising amount of money would come out of the woodwork.

Bruce King
Florence, S.C.

I can think of nothing better for Social Security than to have a portion of it privately funded. As people worry about their taxes, their jobs, and their 401(k) plans, they tend to take Social Security for granted—until it's time to receive it. If it were in part privately funded and their own responsibility, that would force better management and hence a better return on their money.

Eugene P. Beard
New York

Privatizing Social Security to increase saving would not only wreck an irreplaceable government program for fear of "breakdown"—a phony issue—but would also gamble that increased saving will lower interest rates and trigger an investment surge. This is economic faith parading as policy.

Richard B. DuBoff
Professor of Economics
Bryn Mawr College
Bryn Mawr, Pa.

Your proposal to pay for Social Security's transition to a funded system should avoid issuing additional debt. It is irresponsible to pay for today's consumption through obligations on tomor-

row's children. Instead, the transition should be paid for by current workers and retirees through either cuts in government spending or higher taxes. The economic benefits from increased savings and lower interest rates will more than balance these sacrifices.

Maya C. MacGuineas
Cambridge, Mass.

Your program should include the rapid phaseout of taxation of dividends. This tax is a pernicious drain on the rewards of saving and investment that you advocate. It is a second tax on investment earnings already taxed once at the corporate level.

Arthur J. Bryant
Vernon, Conn.

I am not convinced that faster growth will be much help in solving America's economic and social problems. How can it help those with no health insurance? What will it do to improve job skills? Will it make workers worry less about layoffs? Is it going to get the homeless off our streets? Will it reduce pregnancies among unwed teenagers? Will it clean up our streets? Will it rebuild our deteriorated public infrastructure? Will it lead to more equitable distribution of income?

Growth in output will give us more material goods, but that does not necessarily lead to wisdom in solving our economic and social problems.

Ted Sielaff
San Jose, Calif.

You seem to have fallen into this year's fashionable trap: Balance the budget and lessen the tax burden, and all will be well.

There are a number of fallacies in



BEYOND GROWTH
"Growth in output will give us more material goods, but that does not necessarily lead to wisdom in solving our economic and social problems"

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INTERNATIONAL  PAPER

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your argument: First, reducing the federal deficit may not raise national saving. Economists know very little about the determinants of personal saving.

Next: Is personal saving really the constraint on investment spending that you, and a multitude of others, seem to imply? Most standard econometric analyses look at a variety of factors: corporate profits, demand, and the cost of capital.

Finally, will the stock market really soar if some of the Social Security funds are invested in equities? Your conclusion implies that price-earnings ratios will rise significantly if individuals redirect their savings into the stock market, without any change in the fundamentals that determine stock prices.

Your emphasis on raising the rate of long-term growth is commendable. I don't think the policies you advocate are correct.

Arnold Pearlman
Sandy Hook, Conn.

It is clear that Social Security must be fixed. Let's start by abolishing the automatic cost-of-living increases. Make Congress pass all increases and specify how they will be funded. Knowing how Congress works, we will see increases each election period!

David C. Steinberg
Plainsboro, N.J.

Your article was a welcome example of intelligent exposition during a time of uninspiring campaign rhetoric devoid of any genuine long-term solutions to the problems you raise.

Neel Doshi
New York

VIRGIN'S INTENTIONS ARE UNSPOTTED

I must take objection to how you misrepresented Virgin Atlantic's opposition to the proposed marketing merger between American Airlines Inc. and British Airways PLC ("Don't blow this chance to open British skies," *News: Analysis & Commentary*, July 15).

Virgin Atlantic has been one of the biggest proponents of U.S.-U.K. open skies for many years. Our objection to the BA/AA alliance is based on two simple facts. First and foremost, the alliance is in clear violation of U.S. anti-trust law, because the combination represents an average market share of 60% on all U.S.-U.K. routes, and 80% to 100% on certain individual routes.

The second fact is that Heathrow Airport is full. Virgin would love to

CORRECTIONS & CLARIFICATIONS

In "Where LBO Means 'Let's be offbeat'" (*Finance*, July 1), Ghjardelli Chocolate Co. was wrongly described as the world's largest chocolate company. It is the world's oldest.

compete with BA on every route from Heathrow, but we have been denied the appropriate slots in one application after another.

Indeed, it took Virgin nearly four years to obtain the commercially viable slots to operate our recently launched Washington-London service. But BA, which already had a treasure trove of slots, was able to add a second daily service on that route with only a few weeks' planning. Finally, you fail to say that divestiture of Heathrow slots is unacceptable to American. Chairman Robert Crandall at his June 12 press conference stated: "If we are expected to give up slots, this deal will not happen." To my ear, it sounds like American is the one seeking to subdue competition at Heathrow. That is quite a departure from the meaning of "open skies," which I think your publication enviably pursues.

Richard Branson
Chairman
Virgin Atlantic Airways
London

'WHY DON'T WE LET SUPREME COURT JUSTICES JUDGE?'

If the standards for recusal were as strictly adhered to as Stan Crock suggests ("What if a Supreme Court justice prejudices?," *News: Analysis & Commentary*, July 1), the Supreme Court would be hard-pressed to make any decision, for lack of voting justices.

I think a better question for Mr. Crock would be: "Why don't we let Supreme Court justices judge?"

Charles F. Plageman
Richmond, Va.

CRACKING DOWN ON ROGUE FUTURES TRADERS

Greg Burns made some salient observations in "The futures exchanges have learned nothing" (*News: Analysis & Commentary*, July 8). The Chicago Board of Trade and the rest of the U.S. futures industry have demonstrated for quite some time the ability to minimize the possibility of something like the Barings banking fiasco occurring in our

markets. What we continue working toward today is an increased level of coordination and cross-border unity among international regulators and our regulator, the Commodity Futures Trading Commission.

The U.S. futures industry has set the standard that other countries try to emulate. The difficulty, as Mr. Burns correctly points out, lies in improving the level of coordination and cooperation internationally. If parties are intent on committing fraudulent activities, it will be difficult to stop them.

Patrick H. Arbor
Chairman of the Board
Chicago Board of Trade
Chicago

THE REAL ALLURE OF CALLABLE BONDS

Cheers to *BUSINESS WEEK* for looking out for the investor ("Turbocharged bonds—so better buckle up," *Personal Business*, July 8). You were correct in pointing out that callable step-up coupon notes offer minimal price appreciation compared with other noncallable notes. However, the last time I checked, investors did not buy bonds for their price-appreciation potential. Rather, they buy them for the fixed income associated with them. And the income associated with these bonds is higher than with other bonds issued by the same company. In other words, the investor is receiving more of a return without taking on more credit risk.

Tad Henderson
Stone & Youngberg
San Francisco

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THE END OF SCIENCE

Facing the Limits of Knowledge in the Twilight of the Scientific Age

By John Horgan

Addison Wesley • 308pp • \$24

HAS THE UNIVERSE RUN OUT OF SECRETS?

After much pondering, I came up with three reasons why John Horgan has written a book boldly proclaiming that "science... has ended." One is simple expediency. As *Scientific American's* best writer, Horgan has carved out a niche: profiling luminaries of science and the philosophy of science. Most of them are long past their first bursts of youthful creativity. (Indeed, quite a few have died since Horgan interviewed them.) In the author's profiles, these subjects tend to ruminate about their legacies—and life's deeper questions.

In addition, instead of covering real scientific conferences to hear the latest findings on, say, heart disease or geology, Horgan has a penchant for attending rap-session-like gatherings on such fuzzy topics as the limits of knowledge. There, researchers prove that brilliance in science doesn't make them any better equipped than the ancient Greeks to understand the nature of truth.

All of this has left Horgan with notebooks full of fascinating musings about the power and ultimate reach of science. So it's a shrewd move to repack-age his original profiles and stories as a quest to prove that "the great era of scientific discovery may be over." And if many of his subjects don't agree, Horgan, with engaging hubris, retorts that the scientists are misleading themselves.

The repackaging works surprisingly well, creating a compelling tale. It helps, too, that despite the title, the book is much more than an argument that science is ending. A deft wordsmith and keen observer, Horgan offers lucid expositions of everything from superstring theory and Thomas Kuhn's analysis of scientific revolutions to the origin of life and sociobiology. He also delivers on his promise to provide "a series of portraits, warts and all," of top scientists and thinkers. The long list includes lin-

guist Noam Chomsky, biologists Edward O. Wilson, Francis Crick, and Stephen Jay Gould, and physicists John Wheeler and Sheldon Glashow.

He has a knack for revealing description. Of artificial-intelligence pioneer Marvin Minsky, he writes: "With his paunch and vaguely Asian features, he resembled Buddha—Buddha reincarnated as a hyperactive hacker." The search for a pithy phrase, however, can lead Horgan to trivialize ideas and personas. Gould's "view of life can... be summed up by the old bumper-sticker slogan, 'Shit happens,'" he writes, while Stephen Hawking "may be less a truth seeker than... a cosmic joker." But, hey, that's part of the fun.

A second reason for the book is that Horgan's argument is worth making—although his pessimistic conclusion is far too sweeping. It's self-evident that, as Horgan points out, "we can only discover the periodic table and the expansion of the universe... once." It also may be true that "there will be no great revelations in the future comparable to those bestowed upon us by Darwin or Einstein or Watson and Crick." Clearly, progress in some fields, such as particle physics, has slowed or even halted.

But there's no guarantee that the future won't bring important discoveries. After all, every time thinkers have believed they had all the answers, they've been hit with new surprises. Horgan himself admits that finding extraterrestrial life would revolutionize biology. And better particle accelerators, planetary probes, and other scientific tools will undoubtedly turn up revelations.

Even if tomorrow's findings don't measure up to the discovery of DNA's

structure or the theory of relativity, does that mean science has ended? Horgan argues that it does, claiming that what's left will simply be boring detail work. But that fails to take into account how many such details remain to be elucidated—or how important they are. What about figuring out exactly how the intricate dance of genes and carcinogens leads to cancer? Or understanding the physics of tiny bits of matter—thus laying the foundation for tomorrow's electronics? The answers may not be the Ultimate Truth that Horgan craves, but to lesser mortals like me and to thousands of real scientists, there's more than enough intellectual challenge.

Which brings me to my final insight into Horgan's motivations. The book may ostensibly be about limits to science, but the subtext is Horgan's preoccupation with what he calls The Answer—a theory that explains every-

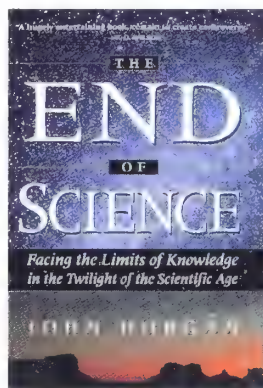
thing. There's much bracing speculation by Horgan's subjects about such a final theory and how it might prove trivial or incomprehensible.

Even while doubting that science can find a final theory, Horgan fears getting too close to one. "The Answer is that there is no answer; only a question," he writes. So the more knowledge we get, the more we must "confront the pointlessness of existence." That explains why "we humans, even as we are compelled to seek truth, also shrink from it," he argues.

Let's hope that Horgan's gloom isn't any more serious than that of Gregory Chaitin, a top IBM mathematician. In one amusing incident, Chaitin proclaims that mathematics is dead, then blames his pessimism on having eaten too many bagels. But all this talk of ultimate truths is a bit too deep for me. I prefer a sentiment Horgan quotes from British neuroscientist and Nobel laureate John Eccles: We must keep "discovering and discovering and discovering.... And we must not claim to have the last word on anything." Not even about the end of science.

BY JOHN CAREY

Senior Correspondent Carey covers science for BUSINESS WEEK.



NO MORE BREAKTHROUGHS LIKE DARWIN'S OR EINSTEIN'S ARE FORTHCOMING, ARGUES HORGAN

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- 8 LEADERSHIP SECRETS OF THE ROGUE WARRIOR** by Richard Marcinko (Pocket Books • \$20) *The Navy SEAL and novelist's commandments for business.*
- 9 THE PATH** by Laurie Beth Jones (Hyperion • \$16.95) *How to plot your own mission statement.*
- 10 CO-OPETITION** by Adam M. Brandenburger and Barry J. Nalebuff (Currency • \$24.95) *Game theory and strategy for a world of changing business rules.*
- 11 THE DISCIPLINE OF MARKET LEADERS** by Michael Treacy and Fred Wiersema (Addison-Wesley • \$25) *Consultants diagnose what successful companies do.*
- 12 THE FUTURE OF CAPITALISM** by Lester C. Thurow (Morrow • \$25) *Is the economic system headed for a new dark age?*
- 13 BUILT TO LAST** by James C. Collins and Jerry I. Porras (HarperBusiness • \$25) *How 3M, Wal-Mart, Procter & Gamble, and others became standouts.*
- 14 THE LOYALTY EFFECT** by Frederick F. Reichheld (Harvard Business School • \$24.95) *How loyalty between management and employees spurs company growth and profits.*
- 15 THE ROAD AHEAD** by Bill Gates, with Nathan Myhrvold and Peter Rinearson (Viking • \$29.95) *Observations on the I-way and a peek at the \$30 million house that Bill built.*

PAPERBACK BUSINESS BOOKS

- 1 THE SEVEN HABITS OF HIGHLY EFFECTIVE PEOPLE** by Stephen R. Covey (Fireside • \$12) *Habitually popular.*
- 2 1001 WAYS TO REWARD EMPLOYEES** by Bob Nelson (Workman • \$8.95) *Give them a champagne brunch, a casual-dress day—or plain old cash.*
- 3 GET A FINANCIAL LIFE** by Beth Kobliner (Fireside • \$11) *Hey, Gen X'ers—mutual funds and mortgages can be fun!*
- 4 THE 1996 WHAT COLOR IS YOUR PARACHUTE?** by Richard Nelson Bolles (Ten Speed Press • \$14.95) *The enduring job-search bible.*
- 5 THE BEARDSTOWN LADIES' COMMON-SENSE INVESTMENT GUIDE** by the Beardstown Ladies Investment Club with Leslie Whitaker (Hyperion • \$10.95) *Recipes for Four-Bean Salad, Five-Hour Stew—and 23% returns.*
- 6 FIRST THINGS FIRST** by Stephen R. Covey, A. Roger Merrill, and Rebecca R. Merrill (Fireside • \$14) *Managing your time by balancing your life.*
- 7 LEARN TO EARN** by Peter Lynch and John Rothchild (Fireside • \$13) *Capitalism for beginners.*
- 8 THE WALL STREET JOURNAL GUIDE TO UNDERSTANDING MONEY AND INVESTING** by Kenneth M. Morris and Alan M. Siegel (Fireside • \$13.95) *Concise explanations enriched with graphics.*
- 9 GETTING TO YES** by Roger Fisher, William Ury, and Bruce Patton (Penguin • \$11.95) *A Harvard team's step-by-step guide to conflict resolution.*
- 10 THE ONLY INVESTMENT GUIDE YOU'LL EVER NEED** by Andrew Tobias (Harcourt, Brace • \$12) *Overcoming "money intimidation," now in an updated edition.*
- 11 JESUS CEO** by Laurie Beth Jones (Hyperion • \$10.95) *That team-builder and turnaround artist from Nazareth.*
- 12 YOUR MONEY OR YOUR LIFE** by Joe Dominguez and Vicki Robin (Penguin • \$11.95) *To achieve financial independence, restructure your life.*
- 13 THE ONE MINUTE MANAGER** by Kenneth Blanchard PhD and Spencer Johnson M.D. (Berkley • \$9.95) *Three management techniques, conveyed in brief story form.*
- 14 HEART AT WORK** by Jack Canfield and Jacqueline Miller (McGraw-Hill • \$14.95) *Personal stories showing how work can be made more humane.*
- 15 PERSONAL FINANCE FOR DUMMIES** by Eric Tyson (IDG Books • \$16.95) *Lighthearted primer.*

BUSINESS WEEK's Best-Seller List is based on a survey of chain and independent booksellers that carry a broad selection of books on economics, management, sales and marketing, small business, investing, personal finance, and careers. Well over 1,000 retail outlets nationwide are represented. Current rankings are based on a weighted analysis of unit sales in June.

HOT TYPE

BUZZ OFF, SUN TZU. THE BUSINESS-AS-WAR crowd has a new D.I.: Richard Marcinko, onetime U.S. Navy SEAL, sometime novelist, and full-time hard-ass. And Marcinko has some words for all you yama's boys: "Attack! Attack! Attack!"

In fact, Marcinko has lots of words for you in *Leadership secrets of the Rogue Warrior*, No. 8 on this month's best-seller list. The secrets are codified in a set of "ten commandments," which range from "Thou shalt do nothing I will not do first" to "The more thou sweatest in training, the less thou bleedest in combat." A chapter of the book is devoted to each of these maxims, with elaboration drawn from Marcinko's combat experiences and from the world of business.

Can desk jockeys truly use this stuff? "I ignored the gunshots and swam on the surface like a piranha out of hell," he writes, illuminating the principle that one must "lead from the front." In the same chapter, we're told how Waldenbooks Inc.'s former CEO, Charles R. Cumello, "bailed out of corporate HQ and dived into the trenches...working the cash registers." To illustrate that "good things usually hurt," we learn of a painful encounter in which "the blast of an AK-47 singed the back of my neck"—and of an executive forced to work "from 7 a.m. until 7 p.m., six days a week, at a furious pace."

Well, why not? Incoming! Man, the phone really rings off the hook on Mondays, doesn't it?

BY HARDY GREEN



ASTROVISION



Panasonic



Imagine three and a half billion hearts pounding as one.

Beginning July 19, the world will be transfixed by a single event -- the 1996 Olympic Games. And thanks to Panasonic Digital Broadcast Video Technology, an estimated 3.5 billion people, the greatest television audience in history, will witness the drama of the games.

From Athens to Zurich, the Arctic to Zanzibar, every place on earth will be able to encounter the dazzling video images and astounding audio captured by Panasonic Digital Technology.

For those in Atlanta, Panasonic will change the way people experience the games while they are at the games. Huge Astrovision® Screens placed in the Olympic Stadium and in other locations in Atlanta will take the energy and excitement of these live events and make them bigger than life.

During the 1996 Olympic Games in Atlanta, all that will separate nations will be fractions of an inch and hundredths of a second.



Atlanta 1996

And throughout the world, people will be joined together by the Olympic spirit and the video technology from one company. Panasonic. We're more than a sponsor. We're part of the team.

Matsushita Electric
Panasonic Technics Quasar

BY STEPHEN H. WILDSTROM

TAKING CARE OF BUSINESS

Intel's Pro and Windows NT are an unbeatable combo for the office

When Intel released its superfast Pentium Pro microprocessor last fall, the chip-maker disappointed many power users hungry for the latest and fastest. Intel said the Pro was for file servers that run networks and maybe a few very high-end workstations. Mere mortals, it added, should stick with the plain old Pentium.

But nothing stays the same for long in the PC world. Intel now pushes the Pentium Pro as "the next wave in business computing." And computer makers are responding by offering mainstream businesses Pro-based desktops that start below \$3,000.

SMOOTHIE. Software explains why these machines are intended mostly for businesses. Intel made the chip to run with operating systems, such as Microsoft's Windows NT or IBM's OS/2, that gulp data 32 bits at a time. Windows 95, the operating system of choice for the home, for small business, and for laptops, is only partly 32-bit software. Win95 runs games and older software that Windows NT can't handle. But while it runs fine on the Pro, Win95 shows little performance gain over a standard Pentium.

Windows NT, however, is a star in the office. Networking is smoother, and it lets computers take full advantage of up-to-date software.

Later this summer, when Microsoft ships NT 4.0 with its Win95-like interface, many businesses will find the Pro-NT combination irresistible.

The OptiPlex gxpro series from Dell Computer Corp. (800 822-1609, www.dell.com) shows why. The basic model sells for \$2,899, including Windows NT 3.51. That's only about \$150 more than a similarly equipped OptiPlex gx with a 166 megahertz Pentium. Intel's tests show that

INSIDE LOOK: *The GXpros' design makes them easy to service*



DELL'S PRO STARS

OPTIPLEX GXPRO 180

180-MHz Pentium Pro,
16-MB RAM,
1-GB hard drive,
15-in. Dell monitor
\$2,899

OPTIPLEX GXPRO 200

200-MHz Pentium Pro,
32-MB RAM,
2-GB hard drive,
8X CD-ROM,
17-in. Dell monitor
\$4,497

OPTIPLEX GXPRO DUAL 200

Two 200-MHz Pentium Pros,
64 MB RAM,
4-GB SCSI hard drive,
8X CD-ROM,
20-in. Sony monitor
\$7,990

DATA: BUSINESS WEEK

the 180 MHz Pentium Pro, the slowest of the breed, runs 32-bit applications, such as Microsoft Office 95, up to 72% faster than a 166 MHz Pentium.

SPEEDSTER. I tested a mid-range system with a 200 MHz Pentium Pro, 32 megabytes of RAM, and a high-end Imagine II display adapter from Number Nine Visual Technology. The display adapter offers speedy performance that is a huge asset when running graphics-intensive programs such as PhotoShop or AutoCAD. Except for some minor networking glitches, I got the preinstalled Windows NT running without hassle. The machine was screamingly fast.

For example, a database search that took 139 seconds on my workhorse 90 MHz Pentium took just 24 seconds on the OptiPlex. If you're doing serious graphics or heavy number-crunching, a dual-processor OptiPlex with gobs of memory and a big monitor will set you back around \$8,000. But the machine can compete with more expensive workstations from Sun Microsystems Inc., Silicon Graphics Inc., and others.

Speed isn't all the OptiPlex gxpro has going for it. Home-computer designers should look at how easy servicing is. The cover comes off without screws. Flip a lever and a cage containing all the add-in cards lifts out, allowing you to add or remove cards without contortions or skinned knuckles. And the power supply is hinged to flip out of the way, leaving the entire system board exposed. In addition, the steel-reinforced plastic case is designed to be completely recyclable.

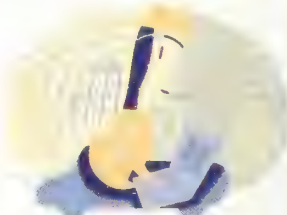
The Pentium Pro still isn't for everybody. But what was exotic technology a few months ago is now poised to become a business workhorse—and one you may well want on your desk.

BULLETIN BOARD

UPDATES

MAPS: DOOR-TO-DOOR ...

As I noted last Dec. 18, trip-planning software does a great job of routing you from one city to another, but usually can't point you to a specific block. RoadTrips Door-to-Door from TravRoute Software (888 872-8768) solves the problem, using its detailed database of local



streets and traffic rules to guide you through those crucial last miles. On the whole, I found the \$80 program's instructions almost uncannily accurate, though it occasionally got tripped up by errors in its database. For example, near my house, it wanted me to use a freeway entrance that exists only as a gleam in the highway department's eye. A possible drawback: The program needs a hefty 50 megabytes of disk space.

... AND EYE-IN-THE-SKY

Map'n'Go from DeLorme (800 452-5931), a more traditional trip planner, might not get you door-to-door but has snazzy features. The \$39 2.0 version includes the American Automobile Assn.'s database of 57,000 restaurants and lodging places. Its best feature: an ability to produce detailed strip maps of a route that look particularly good when printed on a color inkjet. The program can work with a Global Positioning System satellite receiver to track your car's position on a map shown on a laptop.

QUESTIONS? COMMENTS? E-mail tech&you@businessweek.com or fax (202) 383-2125

This Summer Hilton Is

Giving Away 13,000,000 Airline Miles.

That's Kind Of Like Having Your Own Private Jet.



Now there's 13 million more reasons to stay at Hilton this summer. Between July 1 and September 15, thirteen HHonors[®] members with the most qualifying Double Dip[®] stays will earn 1,000,000 airline miles each. And every member can earn up to 3,000 bonus miles too. Just three Double Dip stays with the same airline partner during the promotional period can be worth 1,000 bonus miles, up to nine Double Dip stays for a total of 3,000 miles. Don't wait another minute—start requesting both points and miles with any of these airline partners: Air Canada, Alaska Airlines, America West Airlines[®], American Airlines[®], British Airways, Continental Airlines, Delta Air Lines, Mexicana Airlines, Midwest Express Airlines, Northwest Airlines, TWA[®], United Airlines and USAir. With all those airlines and all those miles, it's the next best thing to having your own private jet. Visit us on the Internet at <http://www.hilton.com/13mm>, or for reservations, call your professional travel agent or 1-800-HILTONS.

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only at HHonors. Excludes partner award stays. Offer valid from July 1 to September 15, 1996. Air Miles to be awarded by September 15, 1996. Only one stay per partner during the promotion. Qualifying stays are stays at business rates for which you earn both points and miles. (consecutive nights at the same HHonors hotel count as one stay) with check-in or check-out dates between 7/1/96 and 9/15/96. Only one stay per calendar day. Hilton will notify qualifier by 12/31/96. In the event of a tie, the member who has earned the greatest number of HHonors Base points during the promotional period will qualify. Only three 1,000 mile (1,000 kilometer on Mexicana Airlines, 100 Air Miles on British Airways U.K. Executive Club Members) bonuses per member in the promotional period. Same member cannot win more than 1,000,000 miles in 12 consecutive months. You must be an HHonors member and an HHonors airline partner program member to receive points and miles. All HHonors and airline terms and conditions apply. Allow 6-8 weeks for bonus miles to be posted to your frequent flyer account; stays must be posted by 9/30/96 to qualify. All taxes are qualifiers' sole responsibility. Qualifiers must sign and return affidavit of eligibility and liability and publicity (where permitted by law) release. Offer void where prohibited, taxed or restricted by law or if award of points and miles is otherwise restricted or prohibited by law. American Airlines and AAdvantage are registered trademarks of American Airlines, Inc. American Airlines reserves the right to change the AAdvantage program at any time without notice. The Hilton logo and logotype are registered trademarks of Hilton Hotels Corporation. ©1996 Hilton Hotels Corporation.

BY GENE KORETZ

STRONG DOLLAR, WEAK EFFECT

U.S. foreign earnings still roll in

It wasn't supposed to happen. After soaring nearly 30% last year, U.S. corporate receipts from foreign direct investment were expected to sag this year because of sluggish global growth and a strong greenback's impact on the dollar value of overseas profits. Instead, first-quarter foreign earnings rose 12% over their year-earlier level, and economist Joseph P. Quinlan of Dean Witter Reynolds Inc. expects them to keep that edge through 1996 (chart).

Quinlan thinks many of the policies that have boosted competitiveness of U.S. companies at home are affecting their foreign subsidiaries. Despite Europe's recessionary climate, for instance, receipts from direct investment there

FOREIGN INVESTMENT SWELLS U.S. CORPORATE COFFERS



(a proxy for foreign profits) hit a record \$35 billion last year. And they rose 6.7% in 1996's first three months, suggesting that "U.S. companies have been racking up significant market-share gains."

Mexico's turnaround also aided U.S. foreign direct-investment receipts. After tanking early last year, such earnings rose 256% in this year's first quarter, to \$830 million—the strongest level this decade. And the pickup in America's investment in Japanese facilities is also paying off. Despite Japan's economic woes, U.S. earnings there last year more than doubled, to \$3.7 billion. And they hit \$1.2 billion in the first quarter of 1996 alone—27% over last year's pace.

Looking ahead, Quinlan sees strong evidence of a synchronized global expansion. Japan's economy is already recovering, Germany is turning the corner, and looser monetary conditions in Europe have set the stage for a general

upturn. Latin America is on the mend, and growth in Central Europe and emerging Asia remains solid.

The upshot, says Quinlan, is that America's huge direct investment abroad—which hit \$96 billion last year—should continue to bolster corporate earnings despite the strong dollar.

IT PAYS TO JOIN THE S&P 500

New stock additions get a boost

When the Standard & Poor's 500-stock index adds or drops a stock, so-called index funds—which mirror the index's composition—adjust their holdings accordingly. And that process, report economists Anthony W. Lynch of New York University and Richard R. Mendenhall of the University of Notre Dame, can create some nifty profit opportunities for smart investors.

Before 1989, S&P used to announce changes in its index in the evening (after trading ceased) of the day before the changes were to take place. Sure enough, prices of stocks added to the list usually surged about 3% the next day, while deleted stocks fell.

To reduce such price shifts, S&P in late 1989 began giving the market about a week's notice before the index changes went into effect. The idea was to give fund managers ample time to act before the switch and thus smooth out any price fluctuations.

Apparently, however, the plan has backfired. According to a new study by Lynch and Mendenhall analyzing all 71 changes in the S&P 500 from March, 1990, to April, 1995, the resulting price movements have increased significantly.

Looking only at "clean" index changes (not resulting from mergers or break-ups), the researchers found that stock prices of additions rose an average 3.2% on the first day after the announcement and a further 3.8% in the intervening week. Once the stocks were added, however, their prices dropped—about 0.75% the first day and 1.25% more over the next week. So they still wound up a net 5% higher.

What's behind these rises? Pointing to the huge growth of index funds and index-investing vehicles, the economists estimate that some 16% of the shares of companies in the S&P 500 are now tied up in index investments. Thus, being added to the index can cause a big decline in the effective supply of a stock—and a nice jump in its price.

AN OLYMPIC ECONOMIC LIFT?

How the games will help

What effect will the Atlanta Olympics have on economic growth? Economist Michael Moran of Daiwa Securities America Inc. notes the Federal Reserve Bank of Atlanta expects 2 million to 3 million visitors to Atlanta in July and early August. At \$1,000 or so per head, that means \$2 billion to \$3 billion in Olympics-related expenditures, plus related travel costs.

The bottom line, says Moran, is that Olympic spending could raise the U.S. economy's third-quarter growth rate by a maximum 0.5%, but probably less. The biggest impact is likely to be in monthly statistics such as the July employment numbers and restaurant sales.

WHERE THERE ARE JOBS GALORE

Small businesses can't fill slots

After months of surprising strength, some observers think employment gains are about to lose some steam. But America's small businesses, which take credit for much of the nation's job creation, see no slowdown ahead.

The National Federation of Independent Business reports that its small-business optimism index surged in June to its highest level all year. At the same time, members' near-term hiring plans hit their highest level in the survey's 23-year history, and a near-record 27% of employers reported difficulty in filling open positions. More members, in fact, griped about problems finding qualified workers than about government regulation.

The best news is that tightening labor markets in the small-business sector don't yet seem to be pushing up either wages or prices. Neither compensation increases nor plans to raise wages in coming months accelerated in June. And plans to raise prices fell by a third from their May level.

THE LITTLE GUYS TURN BULLISH



IS THE BEST INFLATION NEWS BEHIND US?

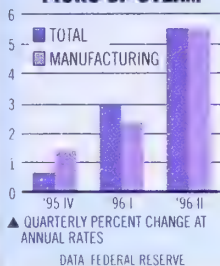
U.S. ECONOMY

If you're worried about all the inflation talk of late, the tame one price indexes probably made you feel better. They also very likely eased your concerns that the Federal Reserve is about to hike interest rates. But if you really want to rest easy, you have to answer a key question: Where will inflation be a year from now?

On that issue, the indicators, while not alarming, are far from reassuring. Not only are tight labor markets pushing up wages, but solid growth in demand, especially by consumers, is keeping homebuilders busy and leading an industrial rebound that may soon strain supply conditions for a wide array of goods (chart). This is the classic environment in which inflation starts to rise.

Barring some dramatic shift in the outlook, such as the current stock-market correction turning into a 1987-style rout, it's a good bet that we are now seeing the best news on inflation for this business cycle. Consumer price inflation for 1996 is on track to rise to at least 3%, up from 2.5% in 1995, and the forces are in place to push the rate higher still in 1997. Inflation is not about to spike up, but it has not posted any acceleration in five years.

INDUSTRIAL OUTPUT PICKS UP STEAM



For Fed policy, the question is: How much of a speedup in prices is it willing to tolerate? Few Fed watchers believe that Chairman Alan Greenspan & Co. will accept a full-percentage-point increase in inflation, but such a rise now looks likely. That's why the markets believe that the central bank is leaning toward hiking interest rates.

The recent instability in the stock market is a new element in the outlook for Fed policy that could stymie any desire to hike rates. Greenspan will be sensitive to the market, especially given the role that higher rates played in the '87 crash. However, the market correction appears to be nothing more than a classic repricing of stocks, based on higher bond yields and more reasonable expectations of earnings (page 24).

THE JUNE PRICE INDEXES at both the wholesale and retail levels looked benign. The producer price index for finished goods rose a modest 0.2% in the month. The core producer price index, which excludes the volatile energy and food sectors, also increased 0.2%. A sharp

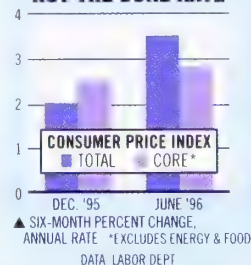
drop in energy costs offset a large rise in food prices.

The story was much the same for the consumer price index. The CPI rose 0.1% in June, while the core index was up 0.2%. Energy prices dropped 2.2% in the month, the most in five years, reflecting drops in both heating oil and gasoline, as runups earlier in the year reversed course. Food costs increased 0.7%, though, the largest advance in a year and a half.

Food is a worrisome component in the price outlook. Wholesale prices of consumer foods in June were up 4.6% from a year ago, the fastest annual increase in six years. The trend will affect retail prices into 1997.

Grain prices have soared, with wheat up 36% from a year ago and corn up 81%, reflecting poor harvests, strong demand, and skimpy stockpiles. Faced with high feed costs, farmers are letting their livestock herds dwindle, so meat prices are also accelerating. The U.S. Agriculture Dept. forecasts that fall harvests will not appreciably relieve the price pressure.

INFLATION IS UP, BUT NOT THE CORE RATE



The Fed will be more interested in the core rate, however, which is less subject to one-time supply shocks in food and energy. In the first half of 1996, core CPI inflation looks tame (chart). It rose at a 2.8% annual rate, vs. a 2.5% pace in the final half of 1995.

For the second half, however, service inflation bears watching, especially with service-sector wages accelerating. Already, core service inflation, 54% of the CPI, rose at a 3.7% annual rate in the first half of the year, up sharply from 2.8% in the final six months of last year. A continuation of that speedup would all but guarantee an acceleration in the overall core rate.

KEY TO THE INFLATION ARGUMENT is the idea that businesses are so busy they can raise prices without worrying too much about losing sales. Certainly, the first part of that proviso was evident in the second quarter. Industrial production climbed in all three months of the spring, including a 0.5% rise in June. Factory output alone increased 0.6% last month.

For the quarter, both total production and manufacturing output grew at an annual rate of 5.5%, the strongest gain in six quarters. As a result, operating rates—an indicator of output bottlenecks that can lead to price hikes—are starting to edge up. Capacity use

for all industries averaged 83.2% in June, up from this year's low of 82.4% in January. The factory rate was 82% last month, up from January's 81.4%.

Operating rates remain below their year-ago levels, because capacity has grown 3.9% over the past year, faster than the 3.5% increase in output. That trend is changing, however. Capital spending is slated to slow in the second half, even as rising exports, solid consumer spending, and the need to rebuild inventories continue to lift production. As capacity approaches 85%, worries about price pressures will heighten.

MANUFACTURING will pick up steam partly because warehouses look empty at many businesses. Total inventories held by manufacturers, wholesalers, and retailers slipped 0.1% in May, while sales jumped 0.7%. The ratio of business inventories to sales fell to 1.37, about equal to the record low of December, 1994.

For retailers other than car dealers, the ratio dropped to 1.41 in May, a 12-year low. The decline means that merchants will increase their ordering this summer, keeping manufacturers busy into the fall. That will apply more pressure on capacity and costs.

Of course, the inventory drawdown is not surprising, given the strength of nonauto shopping in the second quarter. Retail sales slipped 0.2% in June, but that followed a 0.8% jump in May. Car dealers accounted for the June drop-off. Excluding motor vehicles, sales were

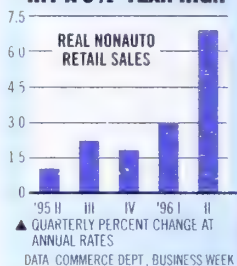
up 0.1%, the fifth consecutive gain. After adjusting for prices, real nonauto retail sales grew at a rousing 7% annual rate in the second quarter, the strongest advance in 3½ years (chart).

Sales of furniture and building materials were a big part of the second-quarter strength, as the housing market shows few signs of succumbing to higher mortgage rates. Housing starts rose 1.3% in June, to an annual rate of 1.48 million, and single-family starts surged 7.4% to a two-year high of 1.23 million.

Retail sales in early July got off to a slow start, according to weekly surveys of chain stores. However, the consumer sector should get a boost from spending related to the Olympics in Atlanta.

The future of demand will be a crucial piece of the inflation puzzle. If spending remains as healthy as it was in the first half, the pressures from wages and other costs will start to fuel consumer prices. Clearly, the Fed and long-term investors do not welcome such a scenario. But absent some drastic shift in the outlook—whether from the financial market or from monetary policy—it is hard to see how the economy will skirt a noticeable upturn in inflation.

WHERE SALES GROWTH HIT A 3½-YEAR HIGH



ITALY

PRODI'S WEAKNESS ROILS THE MARKETS

Prime Minister Romano Prodi's honeymoon with the financial markets is over. The markets had high hopes that Prodi's center-left coalition could deliver a tough fiscal program aimed at European Monetary Union that would give the Bank of Italy added leeway to cut interest rates. Now, Prodi's fiscal agenda is uncertain amid concerns that his Olive Tree coalition is weak. The BOI seems in no hurry to cut rates, even as the economy weakens. And both the stock and bond markets are showing their disappointment.

Prodi has already made concessions to the leftist Communist Refoundation Party, on which his coalition depends for support. In

order to move his three-year economic plan, a broad outline of 1997-99 fiscal policy, through Parliament, Prodi gave in to leftist demands that he protect workers' real incomes and create jobs. The compromise highlights the troubles ahead this fall, when Prodi must submit the details of his 1997 budget. He is also seen to be dragging his feet on the privatization of telecom giant STET in the face of opposition from unions, company management, and members of Prodi's coalition.

At the same time, the economy continues to weaken. Real gross domestic product rebounded 0.5% in the first quarter, after tumbling 1.1% in the fourth, but second-

quarter real GDP appears to have declined. Manufacturing continues to slump amid Europe's sluggishness, the lira's recent strength, and excessive inventories (chart). Weak business investment promises to be a drag as well, reflecting soft demand, sagging profits, the phaseout of 1995 tax incentives, and high borrowing costs. The three-year economic plan projects growth of 1.2% in 1996 and 2% in 1997, but those projections could slip in the face of tight fiscal policy and the BOI's reluctance to ease monetary policy.

Amid slack in the economy, the inflation outlook is bright. Inflation should fall sustainably below 4% in the second half, the BOI's criteria for rate cutting. But lower rates—and 1997 growth—also depend on Prodi's budget success, which looks increasingly doubtful.

MANUFACTURING IS WEAKENING



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from over here...**



**...will do rather well
over here.**

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H A N S O N



Cover Story

A swift-kick correction? Or an ugly bear market? The U.S. stock market has soared for nearly six years without either, defying the laws of financial gravity. But suddenly, the nose of this rocketlike market seems to be pointing almost straight at the ground. In the first two weeks of July, the Dow Jones industrial average shed 344 points, or 6%. The NASDAQ composite index, the most widely followed index of over-the-counter stocks, plunged nearly 11% in the same period. While the selling pressure seemed to abate on July 16 and 17—the Dow pulled out of a 168-point loss, rallied to a small gain by the close on July 16, and picked up 18 points on July 17—many investors and analysts believe they haven't seen the last of the wild gyrations.

There's a good reason for the sell-off. Investors are getting sharply conflicting signals. The strong employment numbers that hit in the midst of the four-day Independence Day weekend raised fears of higher inflation and interest-rate hikes. The following week, bad earnings news from technology market leaders such as Motorola Inc. and Hewlett-Packard Co. suggested that earnings were slowing sharply (page 28). The fear, says Edward P. Nicoski, market strategist at Piper Jaffray Inc., is that "you could end up with the worst of both worlds—higher inflation and lower earnings."

Thanks to that one-two punch, investor talk turned from

an economy that was so strong it could trigger inflation to one so fragile it was about to slide into recession. "In just a week, we've gone from a period in which every piece of news is interpreted bullishly to one in which everything is interpreted negatively," says Byron R. Wien, Morgan Stanley & Co.'s U.S. investment strategist, who turned bearish in May. Indeed, many commentators now have little good to say about stocks at all. "If I had to draw a list of the positive and negatives on stocks," says Benjamin Zacks of Zacks Investment Research, "I couldn't think of anything to put in the plus column." The volatility also roiled international markets, several of which dropped 3% or more in sympathy.

DOW JONES INDUSTRIAL AVERAGE

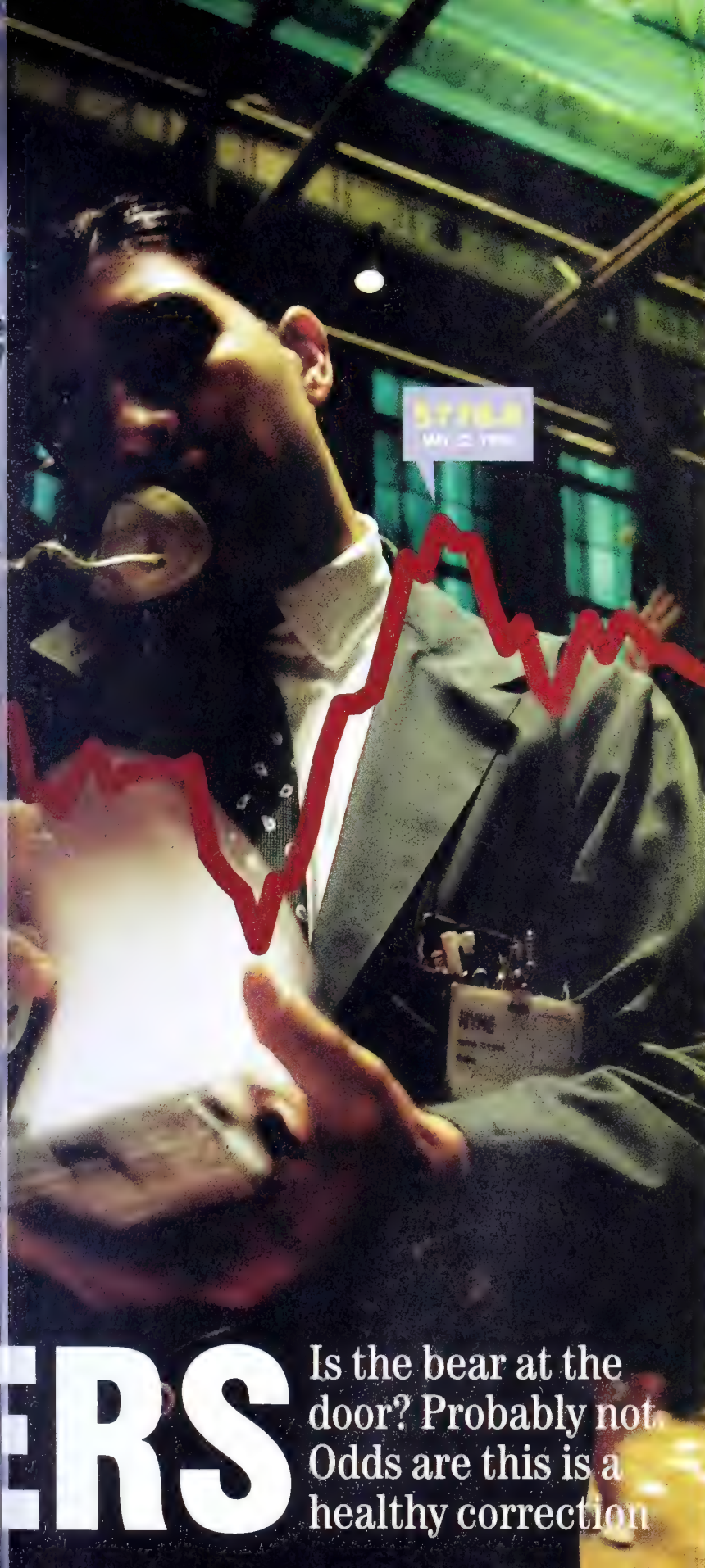
Still, for all the turmoil, the odds are that this is a correction and not the beginning of a bear market. To start with, earnings are still coming in strong, with positive ones beating negative surprises by about two to one. Good profit reports are coming from a range of blue chips such as Caterpillar, General Electric, Ford Motor, and Philip Morris. Even the battered tech sector has some bullish bright spots, including Intel and Computer Associates (page 30).

Even more important, the underly-

MARKET



JIT



ERS

Is the bear at the door? Probably not. Odds are this is a healthy correction

ing economy is still sturdy. True, economic growth is slowing, but it should still remain above 2% in the second half of the year. Although wages are moving up after being dormant for five years, inflation remains under 3%. Employment growth is strong, and the jobless rate, at 5.3%, is the lowest in six years. **FACT OF LIFE.** Perhaps even more amazing is that the White House is now expecting the U.S. budget deficit to come in this year at \$117 billion, a 15-year

low. That's also 1.6% of gross domestic product, the deficit's smallest share of the economy since 1974 and the lowest of all the major industrial nations. "There's just no reason for a bear market," says mutual-fund manager David D. Alger of Fred Alger Management Inc.

Corrections, quite simply, are just a fact of market life: a few steps forward, one step back. The problem is many investors—especially those new to the market—have forgotten that. Since 1990, a year during which Dow Jones industrials dropped over 20%, all of the pull-backs have been under 10%.

Actually, a correction now could obviate the need for one of the things that has concerned investors most: the chance that an overly strong economy

JULY 17, '96	% CHANGE FROM DEC. 31, '95	% CHANGE FROM PEAK
DJIA	5.1	-6.9
NASDAQ	3.3	-13.0
S&P 500	3.0	-6.6
NIKKEI*	7.8	-5.5
*YEN DATA: BLOOMBERG FINANCIAL MARKETS		

PHOTOGRAPH BY ALEX QUÉSADE MATR X CHAPT BY ALBERTO MENA BW

would result in a tighter monetary policy. Federal Reserve Chairman Alan Greenspan appears to have put off a decision on an interest-rate hike until August. But if the chill running through the stock market makes consumers and business more cautious, the Fed may be able to avoid raising rates altogether. "The market correction could slow the economy, which is just what the Fed

Cover Story

wanted," says John E. Silvia, chief economist at Kemper Zurich Investments.

All in all, a correction of moderate proportions—perhaps 7% to 10%—wouldn't be so bad. In fact, such drops are called corrections because they wash out speculative excesses that build up in a bull market. And this stock market, up nearly 60% in the last 20 months alone, has had more than its share of froth. Look at the high-flying technology sector, where until recently, newly public companies such as Prism Solutions Inc. and Red Brick Systems Inc., both in the red-hot data warehousing business, have traded at prices that were several hundred times projected earnings. Both are now down 60% from their highs.

GROWTH ENGINES. How this market slide plays out will have major consequences far beyond the ups and downs of the Dow. High stock prices have given Corporate America access to cheap capital that's feeding an investment and acquisition boom. The bull market has also given small companies, the engines of U.S. job growth, the ability to sell stock to the public and obtain the funds they need to grow. Over the past two weeks, though, dozens of companies, including a high-tech investment bank, Hambrecht & Quist Group, and a high-tech publishing operation, Wired Ventures Inc., have put their plans for initial public offerings on ice.

If the IPO market shuts down, some companies that are still private, such as Boulder (Colo.)-based Wild Oats Markets Inc., which was hoping to go public before yearend, may have to change their plans. "Maybe this will only affect high tech," says Michael C. Gilliland, CEO of the health-food retailer. "But we're keeping our options open. We're looking at debt financing and private money as well." Christopher R. Hassett, CEO and president of PointCast Inc., which develops software that allows users to get customized information and news from the Internet, is in close touch with his investment bankers, carefully tracking the course of high-tech stocks and trying to determine how it will affect his company.

On Main Street as well, the health

HOW TO RIDE OUT THE MARKET'S GYRATIONS

DON'T PANIC If you're well-positioned in light of your investment objectives, don't try to jump in and out of the market. Historically, over 10-year periods, stocks have always recovered and outperformed other investments.

DIVERSIFY There's nothing like a correction to reinforce the importance of owning multiple asset classes. It's the best way to reduce risk and enhance returns. So make sure your holdings include everything from growth stocks to income producers.

DATA BUSINESS WEEK

REBALANCE Find your ideal mix of stocks, bonds, and other assets, then sell your winners and add to your losers to get to it. In an equity correction that usually means buying more stocks.

HUNT FOR BARGAINS Use the slide in prices to pick up stocks in battered sectors such as technology. Also watch for a second look: Financial services, pharmaceuticals, and energy.

LOOK OVERSEAS A stable dollar and rapidly growing overseas economies mean investors will likely get more bang for their buck outside the U.S. And emerging markets, down 20% during 1994 and 1995, are presently outperforming the U.S.



BEAMED IN BOSTON: In the past 18 months, the public has poured some \$200

billion into equity mutual funds, making them the principal source of cash for the bull market. If those investors pull out, the con-

sequences for the market could be dire.

In fact, many investment pros are more worried about the reaction of individual investors to the market's move than they are about any earnings report or rate forecast. "That's what's on everyone's mind," says Abby Joseph Cohen, investment strategist at Goldman Sachs & Co., of her institutional investors. "Their big concern is what happens if individual investors stop buy-

RADE YOUR PORTFOLIO Now is the time to buy stocks of higher-quality companies with proven earnings records. "concept" companies without profits or one-idea wonders.

VALUE, NOT GROWTH If stock prices continue to drop, value managers provide downside protection, since they focus on lower-priced stocks, many of which pay dividends.

FORGET TAXES Before you realize your profits and run, keep in mind that much of what you'll net after paying capital gains taxes from the long bull market. What is left after owing in taxes may outweigh what you lose in any short-term market correction.



g, or worse, if they start to redeem their mutual-fund shares."

If individuals start pulling out en masse, fund managers would have to start dumping stocks just to meet redemptions, which in turn would cause prices to go down, triggering a deadly spiral of falling stock prices. At Charles Schwab & Co., net redemptions amounted to \$700 million on July 16, almost certainly a record. Domestic equity

funds took the brunt of the redemption activity. But fund managers—especially those of the most aggressive, risk-taking funds—have been building reserves as a bulwark against that scenario. "I talked to 50 fund managers in the last day, and they're all ready with cash for redemptions," says market-timer Douglas Fabian, who gave a sell signal to his newsletter subscribers on July 15. Fabian says investors with \$1 billion in assets follow his buy and sell signals.

Indeed, for now, most investors seem to be sitting tight. The net asset value of the hard-charging PBHG Growth Fund, which buys growth stocks with high price-earnings ratios, is down 21% since late May, but investors are not bolting. The total outflow from the \$6.5 billion PBHG fund family hovered around \$20 million a day on July 12 and July 15, according to Gary L. Pilgrim, the fund's manager. And Pilgrim says he had amassed \$750 million in cash anyway in anticipation of the earnings reporting season—so he's got plenty on hand if investors want to bail out.

SILENT PHONES. Many brokers say their phones have been surprisingly quiet. "I have maybe 300 clients, and I've had three calls today," says Christopher Getman, a first vice-president at Merrill Lynch & Co. in New Haven. So far, individual investors are approaching the sell-off with a wait-and-see attitude. Robert J. Fendell, 70, a retired public-relations manager in Jacksonville, Fla., hasn't called his broker yet, but he's keeping up with the market via cable TV and will give it a few more days to see what course it takes. "I can't afford a catastrophic loss," he says. If the situation is still bleak, "I'm going to go for safer ground."

But numerous individual investors say they just plan to wait out the pull-back like a nasty summer storm. "I'm a little jittery," says John O'Neil, 30, of Arlington Heights, Ill., a manager of real estate valuation in the Cook County Assessor's Office. "But I'm in it for the long term, and I didn't consider selling anything"—even his aggressive tech mutual funds. And for some, the correction could play right into their hands. Retired dentist Herbert I. Chauser, 76, of Miami, says he was planning to shift a big chunk of his portfolio from

bonds to stocks anyway—and may now get a chance to do so at lower prices.

Chauser may do well to look for bargains abroad, as well. Wall Street's travails have been echoed on foreign bourses, with Frankfurt, for one, falling more than 3% on July 16 and giving up about a quarter of its gain this year as Wall Street teetered on the brink of a 160-point rout. "We all know that when the Dow has a major hiccup, it'll be felt in other markets," notes Mark Richardson, chief investment officer at Chase Asset Management. The Swiss and Italian markets were hit hard, too. The Mexican *bolsa*, still trying to recover from the peso funk, took a 3% hit on July 15.

Foreigners are also major investors in the U.S. market, though, and trying to catch the dollar's strengthening, they have come to Wall Street in droves. Should the market stumble badly, investors such as Klaus Kaldemorgen, head of international equities at DWS, the mutual-fund arm of Deutsche Bank, could bolt. "We don't yet feel forced to sell," he says. Instead, he has been upgrading his portfolio, adding stronger stocks such as Citicorp, Intel, Federal National Mortgage, and Philip Morris.

Indeed, it's tough to dodge a correction, and many investment advisers recommend that investors go bargain-hunting. Lehman Brothers strategist Jeffrey M. Applegate sees good buys among banks and other financial stocks, which continue to knock out strong earnings gains even in the face of higher rates—among them Chase Manhattan, NationsBank, and J.P. Morgan. Says Applegate: "We're seeing double-digit earnings growth, double-digit dividend growth, and single-digit p-e ratios."

Of course, bargain hunters have some time to do their shopping. The market is likely to remain volatile into early August as earnings reports trickle in. It will also take time for the interest-rate picture to become a little clearer: If a Fed rate hike comes, it will likely do so in August—or not until after the election. Now is not the time to bail out. There is nothing on the horizon to suggest that this correction will be anything but that.

By Jeffrey M. Laderman in New York, with bureau reports

"We've gone from a period in which every piece of news is interpreted bullishly to one in which everything is interpreted negatively"

Low unemployment numbers fan inflation fears

Motorola reports weak earnings, raising tech concerns

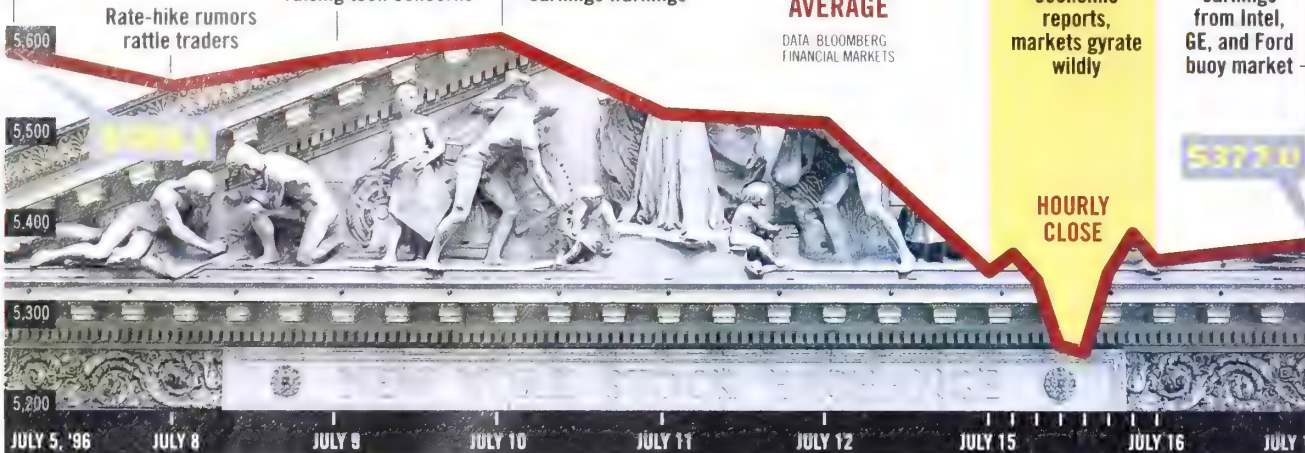
Hewlett-Packard adds to doubts with earnings warnings

DOW JONES INDUSTRIAL AVERAGE

DATA: BLOOMBERG FINANCIAL MARKETS

Despite solid economic reports, markets gyrate wildly

Better than expected earnings from Intel, GE, and Ford buoy market



THIRTEEN DAYS THAT SHOOK THE MARKET

Hot economy, slim profits—no wonder investors were spooked

Ever wonder why Wall Street traders gulp Maalox? July's stunning volatility in the stock market provides a pretty good answer. An unnerving mix of stronger-than-expected economic reports and weaker-than-forecast earnings left even seasoned pros grasping for footing. In the end, bulls and bears staked out their conflicting positions, sending the mar-

Over the next week, investor sentiment underwent a seismic shift. Suddenly, the economy seemed to show signs of softening. The change in mindset was sparked by warnings from some high-profile companies that they would not meet earnings expectations. Late on July 9, Motorola Inc. reported weak earnings, casting doubt on prospects for tech shares. Its stock, which had fallen in after-hours trading on July 9, closed July 10 at 57%, off 8%. The same day, after the market closed, Hewlett-Packard Co. warned its earnings might disappoint. "Fears in the equity market flipped from 'growth is too fast' to 'perhaps growth isn't fast enough to support earnings,'" says Cohen.

"THE CRAZIEST DAY." Earnings fears mounted on July 11, leading to another sharp market fall. At 10:09 a.m., Chicago time, Standard & Poor's 500-stock index futures hit the Chicago Mercantile Exchange's 12-point limit, which temporarily halted trading. Three hours later, the index futures hit the 20-point limit, which had only been triggered twice since its debut in 1990: on Mar. 8, when the Dow closed down 102 points, and on Apr. 8, when it fell 171 points. The July 11 plunge wasn't all that deep—83 points.

Friday, July 12, brought some good news. Subdued producer price index numbers and weak retail sales relieved inflation jitters somewhat. The Dow lost just 10 points. But the weekend gave investors time to worry, and stocks dove on Monday, July 15. The Dow broke

through its 200-day moving average of 5360, which sent an important signal to market technicians, says Scott H. Fulman, chief options strategist at Swiss American Securities Inc. It closed the day down 161 points, almost 3%; the NASDAQ composite index fell almost 4%.

A feeble rally petered out the next morning, and the market seemed to go into a free fall. Intel Corp. was set to report after the close; investors were nervous. By early afternoon, the Dow was down 167.2 points. Again the S&P 500 futures hit the 12-point trigger and the 20-point trigger, halting trading.

There was some good news that day, however. Commodity prices fell, the Fed announced a sharp reduction in the deficit, and some strong earnings reports trickled in. Buying picked up, and the market reversed itself, moving to a 53-point gain before closing at 5358.7 for a 9.25-point gain. "It was probably the craziest day in terms of swings that I've ever seen," says Hogan, because traders couldn't pin the gyrations on any specific announcement or statistic.

The big sellers were money managers. "It was a lot of professional traders and program trading activity," says Hogan. Timothy Heekin, managing director of equity block trading at Salomon Brothers Inc., adds that earnings-momentum selling, moves by asset allocators out of stocks and into bonds, the hedging of options strategies, and mutual-fund redemptions all contributed to the market's swings.

The ride slowed on July 17. Intel had reported strong earnings. Long-bond yields had sunk to 7.02%. The Dow traded within a narrower range and ended the day up 18 points. The NASDAQ index was up a healthy 3.15%. Meanwhile, traders are awaiting signs from the Fed more earnings reports, and pre-election polls. Hold tight, and pass the Maalox.

By Suzanne Woolley in New York with Greg Burns in Chicago

Cover Story

kets up and down in wild gyrations.

The fireworks began on July 5 when the Labor Dept. released a surprisingly strong jobs report. The unemployment rate, at 5.3%, was the lowest in six years. The report also showed a sharp increase in hourly wages, fueling fears of an overheating economy. "The buzz was to keep an eye on the Federal Reserve, that maybe they would [raise rates] before their formal August 20 meeting," says Arthur R. Hogan, head of equity trading at Dean Witter Reynolds Inc.

The market responded as if inflation was set to explode. The 30-year Treasury bond tumbled, and its yield rose from 6.93% to 7.19%. "That fanned fears of a quick, aggressive rise in rates by the Fed," says Abby Joseph Cohen, investment strategist at Goldman, Sachs & Co. Investors dumped stocks, pushing the market down 115 points. The fall was worsened by the lack of liquidity after the July 4 holiday.



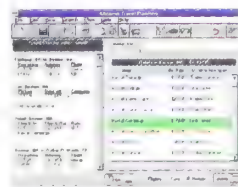
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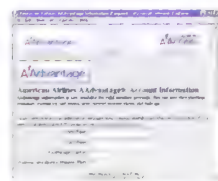
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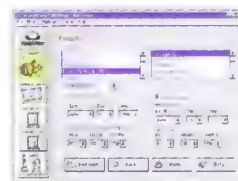
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Online Help



DON'T LOG OFF HIGH TECH JUST YET

The sell-off will separate the strong from the weak

For technology stocks, the past year has been one long roller-coaster ride. As a group, the stocks, most of which trade on the NASDAQ, have nearly doubled in value since 1994. But since last summer, investors have alternately pummeled and praised tech issues over worries that the long tech bull market finally might be over. On July 12, the bottom fell out: The Morgan Stanley High

and the like. "There is a need for a cleansing out of the market and this will do it," says Howard Anderson, managing director at Yankee Group.

PRICE WARS. That's not to say that the stocks of even some very good tech companies won't get whacked around in the next quarter or two. Industry leaders Hewlett-Packard, Motorola, and Applied Materials all contributed to recent broad market jitters by posting disappointing results or making downbeat assessments for the business. "We're going to have to play it a little cautious for a while," says HP CFO Robert P. Wayman. The problem: Parts of high-tech, particularly semiconductors, have been depressed by overcapacity and fierce price competition. At the same time, U.S. computer companies have been dealing with slowing demand in Europe and a strong U.S. dollar that has cut into earnings. Other big companies such as Digital Equipment Corp. and Apple Computer Inc. have big problems, largely of their own making.

But demand remains strong throughout the computer industry. Predicts Benjamin M. Rosen, chairman of Compaq Computer Corp.: "The rest of the year will be pretty good." When the Houston company reports its earnings on July 24, it is expected to post a second quarter profit of \$250 million, flat with last year. But analysts predict profits will rise in the second half of the year, as new computers hit the market.

Technology Index of 35 companies plunged nearly 10% by July 15. Pessimists figured that was it: The tech boom was breathing its last breath.

Don't push the sell button yet. As in the broad markets, what's going on in tech stocks is a market correction. Investors are casting a critical eye on overvalued, overhyped issues—particularly Internet stocks. "You had companies with no revenues that were coming public at valuations of \$500 million and trading up to \$1 billion that were clearly ahead of themselves," says W. Russell Ramsey, president of investment bank Friedman, Billings, Ramsey & Co.

But there's no significant downturn in the all-important computer business, and most high-tech segments are fundamentally solid. In the end, the tech sell-off is a healthy separation of the strong—Intel, Microsoft, and Compaq—from the weak—frothy Net startups

BUSINESS WEEK's REPORT SECOND-QUARTER EARNINGS

CURRENT QTR. SALE
(MILLION)

INDUSTRIALS

ABBOTT LABORATORIES	2,699
AK STEEL HOLDING	575
ALCOA	3,413
BOISE CASCADE	1,261
CATERPILLAR	4,180

CHAMPION INTERNATIONAL	1,444
CHRYSLER	15,839
COCA-COLA	5,253
CONAGRA†††	5,982
CORNING	913

CPC INTERNATIONAL	2,513
CROWN CORK & SEAL	2,353
CUMMINS ENGINE	1,316
DANA	2,020
DOLE FOOD	1,041

EASTMAN KODAK	4,117
FORD MOTOR	37,937
GENERAL ELECTRIC	19,066
GENERAL MILLS†††	1,382
GENERAL MOTORS	44,772

GEORGIA-PACIFIC	3,319
GOODRICH (B.F.)	646
INLAND STEEL INDUSTRIES	1,163
INTERNATIONAL PAPER	5,100
JOHNSON & JOHNSON	5,382

LILLY (ELI)	1,698
NIKE†††	1,921
PFIZER	2,661
PHILIP MORRIS	17,509
REEBOK INTERNATIONAL	817

ROCKWELL INTERNATIONAL††	3,489
RUBBERMAID	573
SHERWIN-WILLIAMS	1,145
TRW	2,728
WHIRLPOOL	2,272

SERVICES

AMR	4,550
BANKAMERICA	N
BARNETT BANKS	N
CHASE MANHATTAN	N
CITICORP	N

DOW JONES	630
ENRON	2,960
FEDERAL EXPRESS†††	2,737
FIRST CHICAGO NBD	N

In Darwinian terms, the strong are getting stronger. Take Intel, which supplies nearly 90% of all the chips used in PCs. On July 16, the chipmaker announced that revenue in the second quarter rose to \$4.62 billion, up 19% from last year's \$3.89 billion. The news triggered a rebound in high-tech stocks on July 17. "This record suggests that demand for high-performance personal computers is fundamentally healthy," Intel CEO Andrew S. Grove said in a statement.

Going forward, the sales outlook, indeed, remains robust. Although the growth of the PC industry is slowing from its 25%-to-30% rates, the over-

earnings reports from 83 companies are actually slightly better than analysts' expectations. But a 30% rise in profits of technology companies from the year-ago quarter has set the markets on edge.

	% CHG.	EST. EPS (5/16)	REPORTED EPS	DIFF.		CURRENT QTR. SALES (MILLIONS)	% CHG.	QTR. PROFITS (MILLIONS)	% CHG.	EST. EPS (5/16)	REPORTED EPS	DIFF.
	+13	0.93	1.00	+0.07	GANNETT	1,208.7	+19	150.0	+8	1.07	1.07	—
	+11	0.59	0.60	+0.01	HILTON HOTELS	470.0	+11	59.2	+12	1.12	1.20	+0.08
	-51	1.24	1.24	—	MARRIOTT INTERNATIONAL	2,352.0	+11	75.0	+27	0.53	0.55	+0.02
	-40	1.21	0.99*	-0.22	McGRAW-HILL	710.9	0	57.2	+8	0.59	0.57	-0.02
	NM	0.02	-0.55	-0.57	MERRILL LYNCH	6,190.0	+11	433.0	+53	1.55	2.19	+0.64
	+16	1.63	1.94	+0.31	MORGAN STANLEY GROUP	1,528.0	+51	301.0	+81	1.23	1.75	+0.52
					MORGAN (J.P.)	NA	NA	440.0	+40	1.70	2.14	+0.44
	-92	0.44	0.16	-0.28	NATIONS BANK	NA	NA	605.0	+30	1.95	1.98	+0.03
	+668	1.35	1.38	+0.03	OFFICE DEPOT	1,381.4	+15	28.2	+3	0.19	0.18	-0.01
	+17	0.42	0.42	—	PAINWEBBER GROUP	1,431.2	+7	92.2	NM	0.70	0.86	+0.16
	NM	0.69	0.71*	+0.02	SAFEWAY	3,945.4	+5	106.7	+55	0.42	0.44	+0.02
	NM	0.49	0.41	-0.08	SCHWAB (CHARLES)	491.8	+44	70.1	+58	0.27	0.39	+0.12
	+8	1.07	1.04	-0.03	STUDENT LOAN MARKETING	NA	NA	103.0	+17	1.62	1.79	+0.17
	+99	0.73	0.77	+0.04	TIME WARNER	2,139.0	+12	-31.0	NM	-0.24	-0.26	-0.02
	-36	1.05	1.10	+0.05	TRAVELERS GROUP	5,426.2	+19	575.7	+42	1.02	1.17	+0.15
	+3	0.88	0.90	+0.02	WELLS FARGO	NA	NA	363.0	+56	4.40	3.61	-0.79
	-16	1.07	1.05	-0.02								
	+17	1.23	1.30	+0.07	TECHNOLOGY	33,598.2	+6	2,159.7	-30	0.61	0.56	-0.05
	+21	1.06	1.56	+0.50	ADVANCED MICRO DEVICES	455.1	-29	-34.7	NM	0.09	-0.25	-0.34
	+11	1.14	1.15	+0.01	APPLE COMPUTER††	2,179.0	-15	-32.0	NM	-1.11	-0.26	+0.85
	NM	0.46	0.49	+0.03	ASCEND COMMUNICATIONS	123.3	+332	29.8	+458	0.19	0.24	+0.05
	+1	2.42	2.65	+0.23	CASCADE COMMUNICATIONS	80.4	+176	16.7	+217	0.26	0.17	-0.09
					COMPUTER ASSOCIATES INTL.†	792.1	+37	119.8	+35	0.69	0.32	-0.37
	-96	0.05	0.11	+0.06	ELECTRONIC DATA SYSTEMS	3,497.8	+19	-326.5	NM	0.50	0.51*	+0.01
	-14	0.57	0.70	+0.13	GENENTECH	243.8	+5	21.7	-42	0.31	0.18	-0.13
	-42	0.40	0.65	+0.25	HUGHES ELECTRONICS	4,062.5	+9	306.6	+6	0.74	0.77	+0.03
	-69	0.33	0.33	—	INTEL	4,621.0	+19	1,041.0	+18	1.08	1.17	+0.09
	+20	0.59	0.60	+0.01	MOTOROLA	6,835.0	-1	326.0	-32	0.70	0.54	-0.16
	+12	0.64	0.63	-0.01	NATIONAL SEMICONDUCTOR†††	612.4	-9	9.1	-89	0.17	0.07	-0.10
	+38	0.97	1.06	+0.09	ORACLE†††	1,464.1	+44	266.3	+47	0.38	0.40	+0.02
	+27	0.60	0.61	+0.01	RAYTHEON	3,111.9	+11	209.4	+7	0.89	0.88	-0.01
	+15	1.96	1.97	+0.01	SEAGATE TECHNOLOGY†††	2,014.5	-3	101.0	-10	1.10	0.84	-0.26
	-7	0.27	0.27	—	TEXAS INSTRUMENTS	2,845.0	-12	76.0	-73	0.70	0.39	-0.31
					3COM†††	660.3	+39	29.5	-46	0.46	0.17	-0.29
	+21	0.98	1.02	+0.04	UTILITIES & TELECOM	19,515.6	+8	2,290.4	+12	0.69	0.70	+0.01
	+55	0.31	0.30	-0.01	AMERITECH	3,740.0	+11	567.0	+13	1.00	1.02	+0.02
	+12	0.94	0.95	+0.01	BELLSOUTH	4,620.0	+5	629.0	+13	0.62	0.63	+0.01
	+6	1.90	1.94	+0.04	COLUMBIA GAS SYSTEM	582.4	+28	8.2	-73	-0.09	0.15	+0.24
	0	0.81	0.70	-0.11	GTE	5,293.0	+7	642.0	+10	0.66	0.66	—
	+30	1.20	1.36	+0.16	KANSAS CITY POWER & LIGHT	226.2	+10	27.7	+48	0.40	0.43	+0.03
	+53	3.03	3.20	+0.17	SPRINT	3,506.0	+12	316.5	+30	0.75	0.73	-0.02
	+12	1.76	1.84	+0.08	UNICOM	1,548.0	-1	100.0	-8	0.48	0.47	-0.01
	+6	1.41	1.42	+0.01								
	+17	1.74	1.80	+0.06								
	+12	1.82	1.86	+0.04								
	+5	0.53	0.54	+0.01								
	+24	0.40	0.46	+0.06								
	+32	1.57	2.01	+0.44								
	+9	1.05	1.10	+0.05								

† First-quarter results
NM = not meaningful

†† Third-quarter results
NA = not available

††† Fourth-quarter results
*EPS adjusted for special items

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES. EARNINGS ESTIMATE DATA PROVIDED BY I/B/E/S INTERNATIONAL INC., NEW YORK, NY. I/B/E/S IS A REGISTERED TRADEMARK OF I/B/E/S INTERNATIONAL INC.

market will still expand by a healthy 6% to 20% this year, market researchers figure. For the top-tier PC makers, such as Compaq, HP, and IBM, business is looking up. "Our business continues to be very good," says Michael Dell, president of Dell Computer Corp. In fact, Dell says, its shipments for the quarter ended Apr. 30 were faster than the estimated 23% rate for overall PC market at the time.

AMES. Later in the year, most computer companies will benefit from a flood of new-product introductions, including a generation of powerful home PCs that will run dazzling new 3D game

software. Meanwhile, despite Europe's sluggish economic growth, other major economies around the globe are still holding strong. One sign: Mainframe orders, usually a good indication of capital-spending trends, are sound. Indeed, IBM is expected to benefit from a new generation of mainframes it will start delivering in the fall.

In software, the leaders—Oracle, Microsoft, and Computer Associates—continue to do well. On July 17, CA announced that earnings for the quarter ended June 30 surged 35%, to \$119.8 million, on revenues of \$792 million, up 37% from a year earlier. By far the

best-performing PC software maker is Microsoft. For the quarter that ended June 30, many analysts expect it to beat consensus estimates that its earnings were up 33%, to \$530 million on a 32% gain to \$2.1 billion.

By September, indeed, it may be Microsoft to the rescue: A new version of its Windows NT operating system could prompt a wave of computer buying by customers looking to upgrade. Who knows? By yearend, the tech bull may well be raging again.

By Ira Sager in New York, with Paul Judge in Boston, Amy Cortese in New York, and bureau reports

By Toddi Gutner

HOW TO KEEP THE LITTLE GUY IN THE LOOP

After a volatile day of trading on July 16, Intel's stock closed at \$70 a share. Then, an hour later, the chipmaker announced better than expected quarterly earnings. Institutional investors rushed to trade the stock in the so-called aftermarket, and the stock opened the

Cover Story

following morning at \$74. That was nice for big money managers, who were able to take advantage of the late-breaking information. But for individuals, the news came late. They had virtually no way to participate in the aftermarket, which consists of negotiated trades over electronic exchanges accessible only to brokers and institutions. By the time the stock opened on July 17, individuals had lost their chance to ride Intel Corp.'s stock up on the good news.

Unfair? Yes. And it's just the latest example of a pervasive problem—one made more serious by volatile markets, where stock moves can be particularly dramatic. With trading taking place around the globe 24 hours a day, individual investors are increasingly being left behind. Big institutions active in the global markets can take advantage of knowledge gleaned at any time, be it 8 p.m. or 3 a.m., and trade instantly. **REGRETS OFFERED.** Making matters worse, some companies selectively disclose market-moving information to big institutional investors, giving them an even greater edge. Take Bank of New York Co. It created a big problem on June 19, when it told 92 analysts and institutional investors in a 2 p.m. conference call that it would set aside \$350 million to cover expected losses from delinquent credit-card accounts. The bank didn't publicly announce the charge until 4:09 p.m., after the market closed. By then, its shares had fallen 1%, to 52%. "We regret the circumstances of the June 19 announcement," the bank said in a press release issued two days later.

"There was never an intent to advantage or disadvantage any shareholder."

The timing of big earnings announcements and other news is critical to whether everyone has an equal chance to trade on it. Motorola Inc. announced its disappointing earnings at 5:30 p.m. on July 9. In robust after-hours trading by institutions, Motorola's stock dropped nearly nine points, to 57%, by the time the stock opened after a brief delay the next day. "We report our earnings at the end of the day to give our analysts time to study and absorb the information overnight," says a Motorola

lease market-moving information 20 minutes before their exchanges first open for trading. A company's primary stock exchange should act as a watchdog—and it should levy fines for noncompliance. Repeat offenders should be subject to increasing penalties.

THE MORNING BEFORE. Releasing data in the morning could still leave institutional investors with a small advantage. They're able to engage in premarket trading, which works like the aftermarket. But when sensitive information is disclosed while the market is open, it clearly benefits institutions that can pounce on the news and trade more quickly. Moreover, announcing news shortly before the opening gives any investor a limited amount of time to digest the information before exchange trading starts up.

Sometimes, of course, midday announcements must be made—for example, if a company inadvertently discloses information to a few investors. But companies can minimize the advantage that gives institutions. They can immediately prepare a press release and issue it just as their meeting or call comes to an end. In the same vein, if a stock-moving event occurs midday—if, say, a company completes an important acquisition—that critical information should be released to the company's primary exchange immediately and followed up with a press release.

Sure, institutions are still more likely than the little guy to trade immediately on any news disclosed in the morning. But with early announcements, both groups at least will have nearly equal opportunity. "The field will never be fully level because of the ability of institutional investors to access information," observes Louis M. Thompson, president of the National Investor Relations Institute. But responsible disclosures would go a long way toward making it less hilly.

Gutner covers personal finance for BUSINESS WEEK.



spokesman. But it also gives big market players extra time to act.

About one-third of public companies disclose share-sensitive information in ways that may shortchange individual investors, says a survey by the National Investor Relations Institute, an association for investor-relations professionals. "Small investors deserve the same information at the same time as institutional investors," says Gerri Detweiler, policy director for the National Council of Individual Investors. But neither the Securities & Exchange Commission nor the stock exchanges have clear rules on how companies must share sensitive information.

That should change. Companies should be required to publicly re-

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it's one thing all
athletes have in
common.



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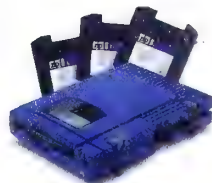
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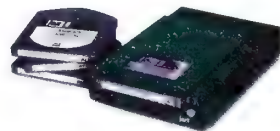
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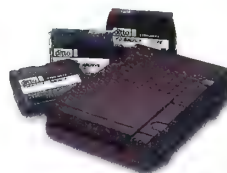
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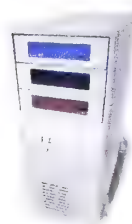
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SPORTS

RUN, JUMP —AND SELL

Commercial exploitation of sports explodes

For the bottled-in-Atlanta Olympics, Coca-Cola Co. is spending \$250 million on its sponsorship, the Olympic torch run, a 20-acre temporary theme park, and advertising and marketing. But never mind that. Three weeks before the games, Coke marketing chief Sergio Zyman was entertaining at soccer's European championships, hanging out the window of a speeding sports car assessing Coke's presence at the Tour de France, calling on global track-and-field king Primo Nebiolo. Days after the Olympic flame dies, he'll host a meeting in France to finalize plans for the 1998 World Cup in France. Says Zyman: "We're moving slowly, inexorably into every sport."

Coke is far from alone. If there's one thing this most commercial of Olympics underscores, it's the exploding corporate exploitation of sports worldwide. With U.S. companies leading the way, sports tie-ins, endorsements, ads, and other promotional ploys have become the linchpin of marketing strategies for companies ranging from Brazil's Brahma brewery to Japan's Sony to Danish brewer Carlsberg. As Philip H. Knight, chairman and founder of Nike Inc.,

notes: "Sports has become the dominant entertainment of the world."

In the U.S., sports-related marketing is a key strategy for such savvy behemoths as Walt Disney Co., which is pouring \$200 million into a new sports complex near its Orlando (Fla.) theme park, and Anheuser-Busch Cos., which is making athletics the backbone of its push to introduce Budweiser beer to global consumers. Worldwide corporate spending on sponsorships alone this year should reach \$13.5 billion, says the newsletter *IEG Sponsorship Report*. The ties between pro sports and business have grown "faster and higher and more explosively than anyone would have thought," says Mark H. McCormack, head of sports marketing group, International Management Group/IMG. "It can't continue at this pace."

NEW STADIUMS. Perhaps it can't. But growth in the big bucks being thrown at sports shows no sign of slowing. Olympic sponsors who squawked at paying \$40 million for worldwide rights to the Atlanta games are lining up to pay \$45 million for Sydney 2000. NBC paid a record \$4 billion for U.S. broadcast rights to the Olympics from 2000

through 2008. New stadiums galore are being built. The National Basketball Assn.'s Michael Jordan just signed a \$5 million, one-year deal with the Chicago Bulls, the richest player contract ever. "There's no way I can justify that contract from a business standpoint," admits Bulls owner Jerry M. Reinsdorf.

The companies betting most heavily on the potency of sports marketing are among the world's most successful (table). Nike taps into the phenomenon by getting endorsement deals with tennis stars such as Andre Agassi and Pete Sampras and Olympic sprinter Michael Johnson by sponsoring events, and even by underwriting professional golfing's junior circuit, the Nike Tour.

And most Olympic sponsors say the bucks were well-spent. "If you do it right, it will result in increased revenues, greater awareness among customers, and insulate you from some of the one-time promotions of your competitors," says David D'Alessandro, head of John Hancock Mutual Life Insurance Co.'s Olympic sponsorship.

International companies are honing sports marketing to a fine—and profitable—art. Brahma Beer bought block-

Sports, Sports, Ever More Sports

ANHEUSER-BUSCH A pioneer in U.S. sports marketing and a huge Olympics sponsor, Anheuser is going global. To back the introduction of Budweiser beer in Europe, Asia, and Latin America, it has quadrupled global marketing dollars this year. Included: overseas ads on ESPN and CNN and tie-ins with regional events worldwide.

COCA-COLA The company now builds most of its marketing programs around sports. In addition to its \$250 million marketing blitz at the Olympics in its hometown of Atlanta, it's making a major investment in promotions involving World Cup soccer, the Tour de France, track and field—even cricket in India.

WALT DISNEY In the past three years, it has bought 25% of the Mighty Ducks, an Anaheim hockey team, and baseball's California Angels. It's building a sports complex near its Orlando theme park, designed to attract families. Other deals range from a pro golf tourney in Orlando to building a kids skating rink in Anaheim.

NIKE Buoyed by the international sports boom, its earnings were up 38%, to \$553.2 million, on revenues of \$6.5 billion, up 35%, in the year ended May 31. It is spending big on promos. It's rumored to be bidding \$200 million to sponsor the Brazilian soccer team for 10 years and is mounting a \$35 million Olympic ad campaign.

By Joan Nesbit

LOOKING FOR MAGIC IN 'THE COKE OLYMPICS'

Runner Joan Nesbit, 34, sister-in-law of BUSINESS WEEK Detroit Bureau Manager Katie Kerwin, has competed four times in the U.S. Olympic Trials. After she missed qualifying for the 1992 Barcelona Games by one place, she had a baby and was hired as a track coach at the University of North Carolina at Chapel Hill. Late last year, she decided to give it one more shot. On June 21, a hot, muggy night in Atlanta, Nesbit qualified for the first time. Her report:

As I head down to the 1996 Centennial Olympic Games to run the women's 10,000 meters in Atlanta, I have mixed emotions. Rather like the Kellogg's Frost-Ed Mini-Wheats commercial, the kid in me wants to shout, "Yippee! It's the Olympics," while the adult in me grumbles, "It's not the same."

Much has changed since the first modern Olympics were held 100 years ago. In 1896, we had Athens; in 1936, there was Berlin; in 1976, Montreal. Just the names evoke the conflict, pageantry, and elegance of sport that I associate with the games. And now in 1996, we have what I call "the Coke Olympics."

TASTEFUL TRINKETS? Atlanta isn't hosting these games, Corporate America is. The athletes and fans won't be trading country pins, they'll be trading company pins: Coke, BellSouth, and IBM. I can't totally knock corporate support (I'm sponsored by New Balance Inc.), but the commercialism in Atlanta is overwhelming.

How overwhelming? In the "sundries bag" I received as an Olympian after the trials last month, I expected to see a few U.S. track-and-field T-shirts, perhaps a throw-away camera. Instead, I unloaded an

unbelievable haul of corporate paraphernalia. There was even a blow-dryer supplied by Conair Corp., emblazoned with stars and stripes.

I suspect athletes in earlier Olympic Games got a few nice souvenirs. And I believe they also got free access to the track stadium on nights when they weren't competing. I know they did in 1964, when unknown U.S. runner Billy Mills pulled the upset of the century in

winning the men's 10,000 meters, because I've read the glorious accounts given by his teammates in attendance.

Such team support will be hard to come by at these games: Athletes get no tickets to other events. I was given just two tickets to track and field on the nights I compete. One will go to my husband and one to my mom. "It's a good thing you only have one parent left," my mother teased. VIPS get most of the best seats using \$10,000

passes provided by companies, while many true fans can't afford to watch—except, of course, on TV, where corporate ads are incessant.

Still, the kid in me wants to believe there's some magic left in the Olympics. I'm excited to march in my first-ever opening ceremony. I look forward to eating meals with athletes from other nations in the Olympic Village.

And I'll admit that my iron cynicism melted when team chaplain Madeline Manning-Mimms, a gold medalist in track three decades ago, sang a gospel tune to the U.S. track-and-field team shortly before we flew to Atlanta. "May the footprints that we leave lead them to believe," she sang. "And may all who come behind us find us faithful." I'd like to remember my Olympic Games that way. I just hope the Coke jingles don't drown out that refrain.



COCKEYED OPTIMIST: Nesbit with daughter Sarah Jane, 3

ASTER: Are business' sponsorship costs spiraling out of control?

soccer seats and dressed fans in Brazil-logo T-shirts to help turn its ad jingle into the unofficial song of Brazil's World Cup championship team in 1994. In Japan, Sony Creative Products is backing J-League soccer by placing \$300 million of J-League apparel in 100 stores nationwide.

MOMENTUM. It seems that almost any sport, in any form, can make a buck on TV. Cable company ESPN's plans for a second sports channel drew predictions of failure when the broadcaster floated the idea. Wrong. "The deuce" has turned a profit. Now, 5,300 hours of sports programming and ownership of one of the world's most popular Web sites isn't enough. "Our viewers are telling us they want more," says ESPN Inc. Executive Editor John A. Walsh. So, ESPN is launching another channel, dubbed ESPN 3.

The Olympics may add momentum to the trend. "Sports lets you get into a dialogue with the consumer without forcing them to buy into the whole gestalt of your product," says Zyman. Coke's marketing is subtle. It invited "community heroes" to carry the Olympic torch, for instance, and designed Atlanta's Olympic City as a place where people can imagine competing in the games. But every aspect of it turns a profit and makes product.

And overkill? Never mind that this is the Olympics in which TV personality Anna White also carried the torch for a time, promoting the game show *Wheel of Fortune*. Zyman insists that "we haven't gone far enough yet in any instance." For the hypermarketers, there is no limit to what sports can do.

By David Greising in Atlanta, with Linda Himelstein in San Francisco, Achary Schiller in Cleveland, Brian Remner in Tokyo, and bureau reports

DEALS

TIME WARNER-TURNER: READY FOR PRIME TIME

Gerald Levin finally gets some good news

For a while, it looked like time might be running out on Gerald M. Levin, CEO of Time Warner Inc. The company's stock has long been lagging, a restructuring announced with much fanfare 18 months ago hasn't materialized, and the company's executive ranks have been in turmoil for a year—especially in its music business and at HBO, its pay-TV service.

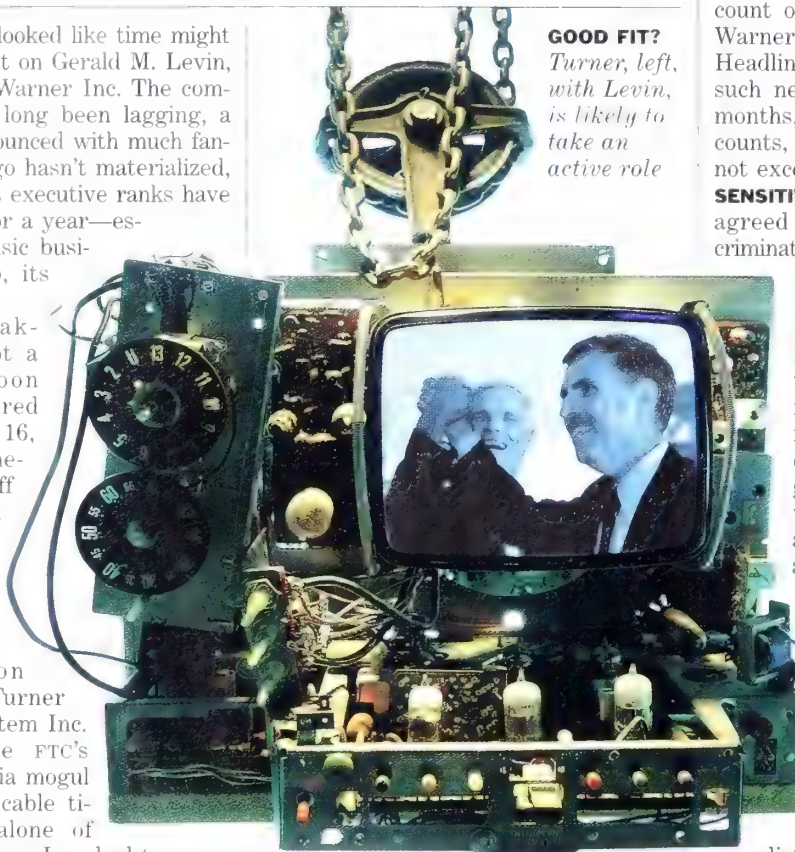
Then, a breakthrough—and not a moment too soon for the beleaguered Levin. On July 16, after weeks of negotiations, the staff of the Federal Trade Commission reached a compromise with Time Warner that would let its \$6.2 billion merger with Turner Broadcasting System Inc. go forward. The FTC's price: Levin, media mogul Ted Turner, and cable titan John C. Malone of Tele-Communications Inc., had to agree to concessions aimed at preventing their new behemoth from squeezing out competitors in cable systems and programming.

BUYING TIME. While the FTC commissioners still have to formally ratify the settlement soon, the merger is expected to be approved, allowing the deal to close by year's end. That's a relief for Levin. Indeed, completing the Turner deal has for the past year been viewed as the cornerstone of his vision for Time Warner. "If the deal had not gone through, it would have been seen as a failed strategy," says Cowen & Co. analyst Harold L. Vogel.

The FTC went for the settlement because it allays fears that Time Warner, Turner, and cable giant TCI (which owns a 21% stake in Turner) would squash rivals in both cable systems and programming. Together, Time Warner and

GOOD FIT?

Turner, left, with Levin, is likely to take an active role



TCI own nearly half of the nation's cable distribution systems. And Time Warner and Turner account for 40% of the country's revenues from cable programming, according to the FTC.

To resolve these concerns, the settlement puts some distance between TCI and the new company. It calls for TCI to spin off its 9.2% stake in the new company into a separate entity owned by TCI's Liberty Media Corp. Malone and

other TCI insiders would be passive investors without voting power or management say. Malone and other TCI officers are even barred from communicating with the management of the new company being formed to hold TCI's Time Warner stock, says a source close to the deal. But analysts figure Malone will still find ways to exert influence.

TCI and Time Warner also will scuttle an agreement that gave TCI a 15% discount over 20 years for popular Time Warner and Turner channels such as Headline News, CNN, and TBS. Now, no such new deals can be struck for six months, there will be no pre-set discounts, and some contract periods cannot exceed five years.

SENSITIVE ISSUE. Lastly, the companies agreed to provisions to prevent discrimination against competing cable programmers and systems. They have agreed not to bundle Time Warner and Turner programming for sale to cable systems, since their popularity might let them raise prices. They have agreed not to discriminate against other cable systems in selling programming. And they will provide other programmers equal access to their systems, including a promise to offer subscriber one of the fledgling cable new channels being launched this year by other media companies to compete with CNN. This is a sensitive issue. In its launch of MSNBC cable, NBC executives have complained that neither TCI nor Time Warner have shown much interest in expanding distribution of the new channel.

Though striking a deal with the FTC is a victory for Levin, there's a twist: It could also mean that he exercises less control over his sprawling conglomerate. With Malone likely to weigh in and with Turner taking an active role at the helm of the company, Levin could find himself gradually edged aside.

That's a plus for some of the company's institutional holders. "[We think John Malone and Ted Turner would be come more active in Time Warner and finally begin to realize some asset value," says John Chadwick, executive vice president of Bessemer Trust Co., holder of 485,000 Time Warner shares. That would be ironic for Levin: His big win with the FTC may only weaken his position as the leader of the rapidly expanding Time Warner empire.

By Catherine Yang in Washington and Elizabeth Lesly in New York

But the deal could mean that Levin will exercise less control over his empire



THE CONVENTIONS

RETURN OF THE CHICAGO SEVEN? NOT LIKELY

To erase memories of '68, city leaders are spending big

The policeman isn't there to create disorder. The policeman is there to prevent disorder.

— Mayor Richard J. Daley, 1968 Democratic Convention

The images are marked indelibly on the nation's conscience. Policemen beating protesters bloody with their batons. Tear gas scattering crowds. TV news broadcasts cutting from Hubert H. Humphrey's nomination to what was called a "police riot" outside the hall. An enraged Mayor Daley mouthing an obscenity at one convention speaker.

The last Democratic National Convention in Chicago, in 1968, showed the city at perhaps its worst since the gangland warfare of the 1920s, and it crippled Humphrey's campaign. "There was this image at Chicago was the city at couldn't allow dissent," says Abe Peck, a '68 protestor and now a professor at Northwestern University.

This time, the Chicago business community and Mayor Richard M. Daley, the former mayor's son, are planning something quite different. In an unprecedented fund-raising drive, business leaders have anted up \$9 million in cash. Some \$4.5

million more in contributed goods and services is expected. The state and city will chip in up to \$13 million, giving the 1996 DNC some \$25 million to reconfigure and beef up security at the United Center, the convention site, and otherwise prepare. "The whole world is going to be looking at Chicago, especially after '68," says Richard C. Notebaert, CEO of Ameritech Corp. and co-chairman of the Chicago '96 committee raising money for the convention. "We ought to make sure the place looks good."

Chicago's appeal to the business community is highly unusual. Most host

POLISHING
For the effort,
71 individuals
and companies
each gave
\$100,000

cities use tax dollars to fund political conventions. But Mayor Daley decided instead to tap corporations through Chicago '96, co-headed by his brother William, a lawyer. The appeal

was double-barreled: Help the city look good while in the spotlight, and plant the seeds for future tourism and convention business.

The pitch found willing listeners. Even companies that don't usually make political donations, including Sears, Roebuck & Co. and Abbott Laboratories, chipped in. All told, 71 companies and individuals gave \$100,000 each, and many others gave less. That contrasts with San Diego, which has raised \$24 million for the Republican convention. Much is from private sources. But many contributions are linked to benefits, such as access to delegate parties, and only \$3.5 million is from local businesses.

SHOWCASE. There's a practical side to the Chicago fund-raising: The DNC is expected to generate \$122 million in local revenues. The city and state will take in an estimated \$24 million in incremental tax revenue. The long-term image enhancement, the city hopes, may be even greater. "There's tremendous potential to make a positive impression," says William Daley.

Mayor Daley plans to use every chance to showcase Chicago to the 35,000 convention visitors. The city is spending \$49 million on infrastructure improvements around the United Center, such as road repair and adding sidewalks. There will be parties, including an Aretha Franklin concert and a reception on the shores of Lake Michigan. The mayor's office will also tout its urban programs, including public school reform and community policing.

Some minor protests are expected. Tom Hayden, one of the leaders of the '68 demonstrations, is planning a commemoration. Others have said they will sleep in Lincoln Park, the scene of nightly clashes between Chicago police and demonstrators in '68. But Mayor Daley is unlikely to repeat his father's mistakes. The city's parks still will close at 11 p.m. But officials say Daley will likely let protesters sleep in the park anyway. This time, you can bet Chicago's Finest will be peacefully looking on.

By Peter Elstrom in Chicago

ELECTION '96

SPRUCING UP THE WINDY CITY

Chicago is cleaning up for the Democratic convention—and will be on its best behavior

BUSINESS Local companies have contributed \$9 million to renovate the United Center, where the convention will be held. Some \$3 million of that will be used to construct a media tent, intended to impress the 15,000 journalists expected to attend. Companies will donate an additional \$4.5 million in in-kind goods and services, such as office space, equipment, and advertising.

ILLINOIS The state will chip in up to \$7 million from its tourism budget for the United Center revamp.

CHICAGO City Hall is spending \$49 million to buff up the blocks around the United Center. It also is planning to give attendees and press guided tours that highlight innovative urban programs. And it will host several big bashes.

DATA: BUSINESS WEEK

By Mike Schroeder

NASDAQ: THE SEC CAN PICK UP WHERE JUSTICE LEFT OFF

The Justice Dept. took a giant leap two years ago when it announced an investigation into alleged price fixing among brokerage firms on the NASDAQ market. The potential cost to investors was billions, according to some studies. But proving collusion is a tall order—and Justice fell short. On July 17, it announced a tepid settlement with 24 firms that had Wall Street claiming vindication. The civil agreement alleges that anticompetitive practices existed but doesn't require any admissions of violations. Firms only had to promise to obey the law in the future and set up trade-monitoring systems.

Still, give Justice credit. The case drew attention to abuses and put in motion still-evolving reforms of the electronic market. "Millions of investors will no longer be subject to the anticompetitive conduct which resulted in higher trading costs," says Attorney General Janet Reno. And in the next few weeks, the Securities & Exchange Commission is expected to make public the results of its own probe of market violations. The SEC needs to send a strong message by issuing stiff fines against wrongdoers and sanctioning the National Association of Securities Dealers for failing to supervise brokers adequately.

POTENTIAL CONFLICTS. Indeed, it's doubly important to crack down on abuses now, when markets are roiled. Otherwise, investors, especially new ones, may take their money elsewhere. Since January, Americans have invested an average of \$23.4 billion a month in equity mutual funds, up from an average of \$10.6 billion a month in 1995. As more workers manage their own retirement money, individual investors' influence will only grow.

That's already happening. For ex-

ample, small investors today get better deals on some NASDAQ stocks. Each NASDAQ stock has an average of 11 securities firms operating as market makers. They post "bid" and "ask" prices for stocks and make money from the spread between the two prices. And since the probe was announced, spreads have narrowed on many of NASDAQ's most



The recent crackdown on abuses fell short, but stiff fines from the SEC would reassure investors

NASDAQ STAFFERS CHECKING TRADES

active issues, according to Justice.

Before Justice launched its investigation, the SEC had grown too cozy with regulatory counterparts at the NASD, which serves as the first line of regulation and the operator of the market. But after Justice began its probe, the SEC followed suit. The NASD and SEC are now in settlement talks.

The SEC already has pressured the NASD into significant reforms. Last November, the NASD board accepted a reorganization plan from a panel headed by former Senator Warren B. Rudman (R-N. H.). To separate trading from market oversight, the NASD has become a holding company with two units: the NASDAQ market itself and an entity called NASD Regulation Inc.

Now securities regulators should follow through on issuing new trad-

ing rules that will level the playing field for small investors. SEC staffers are mulling the proposals and are expected to recommend some form of proposed new rules to the commission by summer's end. "This will strengthen NASDAQ," asserts SEC Chairman Arthur Levitt Jr.

The rules will ensure that small investors in all markets have the same access as the pros to the best stock prices. Currently, the exchanges, which set prices by an auction system, come much closer than NASDAQ to creating a level playing field. Offering better prices to small investors on NASDAQ will take a chunk of trading profits out of broker-dealers' pockets. But the rules could also force NASDAQ to become a true national electronic market, instead of a collective of brokers who get together and decide on prices.

DUAL ROLES. And NASD must better police its own market. The existing system is rife with potential conflicts of interest because the NASD has

dual roles in overseeing 5,400 brokerage firms with more than 500,000 brokers. The new enforcement organization won't be an improvement unless the NASDAQ subsidiary and its district committees aggressively refer rule-breakers for disciplinary action and impose stiff fines and penalties.

Such changes would mark a positive turn for both NASDAQ and other markets served by NASD members. After all, explosive growth has already turned NASDAQ into the second-largest market in the world, after the New York Stock Exchange. Any loss of investor confidence could be dangerous. That's why Justice's two-year pursuit wasn't as futile as it might seem.

Schroeder follows market regulators in Washington.

After the world throws
a party, who
cleans up?



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it'll be good, *clean*
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INTERNATIONAL  PAPER

We answer to the world

EDITED BY KELLEY HOLLAND

METRO-GOLDWYN-MAYER-KERKORIAN?

IN HIS VEGAS GAMBLING DAYS, billionaire Kirk Kerkorian limited himself to three bets per sitting. Three seems to be his magic number again: For the third time since 1970, he is taking control of the famed if faded Metro-Goldwyn-Mayer studio. By backing Chairman Frank Mancuso's \$1.3 billion bid to buy MGM from French bank Crédit Lyonnais, Kerkorian is gambling Mancuso can continue the studio's comeback so it can go public eventually. For now, Mancuso has MGM on a roll with such hits as *Get Shorty* and *The Birdcage*. How long will Kerkorian, who provided an estimated \$700 million of Mancuso's funds, stick around? In his previous tours,

the reclusive billionaire sold the studio twice. His overall take from the two deals was more than \$1.5 billion.

JUDGMENT DAY IS COMING TO ADM

A YEAR AFTER THE GOVERNMENT made public its probe into alleged price-fixing by Archer Daniels Midland, the investigation is about to yield a series of indictments. ADM Vice-Chairman Michael Andreas and Group Vice-President Terrance Wilson have been notified that criminal indictments will be filed against them in September, and the company expects its own set of charges soon, according to sources close to the case. Sources say a special ADM board committee wants to negotiate a settlement. But a plea would effectively jettison two of the company's most senior managers.

SANCTIONS: THERE'S ALWAYS MANANA

CUBA AND ITS U.S. TRADING partners got a reprieve from a measure enacted to pressure Fidel Castro's regime. The sanctions call for lawsuits against foreign companies and individuals who use American-owned property confiscated by Cuba's government. But on July 16, President Clinton delayed the date for filing the suits from Nov. 1 to Feb. 1. Republicans such as Senator Jesse Helms (N.C.) are angry. But Clinton mollified Cuban-American groups by saying that anyone who uses expropriated property after Nov. 1 would be liable if suits are finally allowed.

HOLLYWOOD SHUFFLE AT SONY

THERE'S A NEW ROUND OF executive shuffling under way at Sony Pictures Entertainment.

HEADLINER: RONALD PERELMAN

SORRY, RON. THANKS FOR PLAYING

Billionaire investor Ronald Perelman tried for weeks to buy King World, distributor of such hit TV shows as *Jeopardy*, *Wheel of Fortune*, and *The Oprah Winfrey Show*. The move was meant to provide critical programming for his New World Communications, which had produced a string of clunker TV shows, had run up nearly \$1 billion in debt, and was gushing red ink.

But then, at Allen & Co.'s annual mid-July media conference in Sun Valley, Idaho, lightning struck. News Corp. Chairman Rupert Murdoch, possibly

spurred by Perelman's overture to King World, reopened talks to buy New World. Previous negotiations had stalled in March. Murdoch, who will pay an estimated \$2.48 billion for the 80% of New World he doesn't already own, covets New World's Fox affiliates and the 40% of the country they cover.

Perelman, meanwhile, gets out from under New World and its problems. That leaves him free to pursue a bid for part of the huge Atlantic City gambling market. Seems you can win by losing after all.

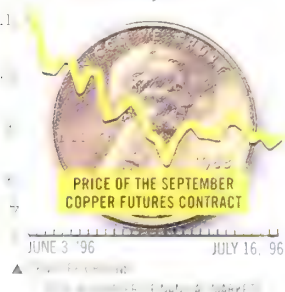
By Ronald Grover



CLOSING BELL

COPPER BOTTOM

The red metal could head deeper into the red. Since the Sumitomo trading scandal broke on June 13, copper futures prices have gone from 99.65¢ to 87.6¢ per pound on July 16. And traders are still fretting over whether the Japanese giant will liquidate the huge inventories it built in a trader's buying spree that soured. "If you didn't have the Sumitomo factor, copper would be over \$1," says David Rinehimer, metals analyst at Smith Barney Futures. He sees copper futures prices as low as 75¢ this year.



ment. Sony Chairman Alan Levine, frustrated by overly slow movie production and excessive spending on marketing by his deputies, is bringing in Home Box Office President Robert Cooper to take charge of Sony's TriStar Pictures unit. Sony marketing chief Sid Ganis is being replaced by Robert Levin, former Walt Disney marketing head, and Columbia Pictures head Lisa Henson is expected to be the next to depart. The changes have set off rumblings that Mark Canton, Sony's overall film chief, could also be on the firing line.

A PACIFIC CROSSING FOR SEGA

SONIC THE HEDGEHOG HAS new management. Sega's Japanese parent company, Sega Enterprises, on July 15 announced that it would send in one of its own executives,

Shoichiro Irimajiri, to be chairman and CEO. The current chairman, Hayao Nakayama, is resigning from Sega America. And President and CEO Tom Kalinske is joining Education Technology, a venture backed by fallen financier Michael Milken and Oracle founder Larry Ellison to promote computers in education. Sega Saturn has done well of late, with a lower price on its 32-bit player. But Nintendo is due to launch a 64-bit player on Sept. 30.

ET CETERA...

- The FCC nixed a request by TCI to use Canadian satellites to reach the U.S.
- Dial Chairman John Teet is leaving, saying Dial's pending split in two ends his work.
- Tribune is buying a \$20 million, 20%, stake in an American Online regional news service.
- Intel and Microsoft inked a deal to let people make voice and video calls over the Net.

DITED BY OWEN ULLMANN

THIS KIND OF 'BIG GOVERNMENT' MAY WIN CLINTON VOTES

Last year, when ruling Republicans in Congress were out to terminate every federal regulation in sight, the Clinton Administration couldn't deregulate fast enough. The Food Drug Administration sped up new drug approvals, the treasury Dept. shelved plans to tighten regs on bank lending to minorities, and all the rulemaking agencies promised a new industry-friendly climate.

But now that it's campaign season, antigovernment Republicans are in retreat and Clinton regulators have a new mantra: Be voter friendly. That's why President Clinton unveiled a meat inspection plan on July 6, why the White House may soon announce new FDA tobacco regulations, and why the president will jawbone broadcasters at a July 29 Oval Office summit about carrying more educational children's shows. All are winning stances with the public, and the GOP Congress can only gripe. These are Mom-and-apple-pie issues," says Brad Stillman of the Consumer Federation of America.

MASS HYSTERIA. The regulatory resurgence goes beyond the high-profile initiatives the White House is promoting. From foul food to unsafe cars, consumer complaints are getting tough with companies that expected a more cooperative stance. "Business feels stabbed in the back," complains Mary Bernard, a lobbyist with the U.S. Chamber of Commerce.

The most controversial of the pro-consumer moves is an FDA plan to cut smoking by kids. The proposal—including a ban on billboard ads near schools and curbs on magazine ads children might see—awaits White House approval. But it has already sparked protests from a broad business coalition. The agency is silencing commercial speech without authority," argues Lawrence Finerman, a lobbyist at the National Association of Manufacturers. The White House sees an advantage in pushing the FDA rules at a time when Republican Presi-

dential candidate Bob Dole is on the run as a tobacco defender.

The tiny Consumer Product Safety Commission hasn't stirred up as much dust as the FDA in policing everyday household items, but it's trying. "We have made this a highly visible agency," boasts Chairwoman Ann W. Brown. She says the CPSC prefers to prod businesses to recall unsafe products voluntarily. But Brown also has forced recalls of such items as flammable rayon skirts and hazardous toys, and she's trying harder to publicize potential dangers. In June, for example, a warning about lead-tainted miniblinds left stores with thousands of returns. "It was mass hysteria," groans International Mass Retail Assn. lobbyist Meg Farrage.



MEAT PLANT: Food safety is a hot button

FRUSTRATED. Likewise, the National Highway Traffic Safety Administration has lately irked auto makers. On June 4, it filed a lawsuit against Chrysler Corp. to order the recall of more than 91,000 1995 Cirrus and Dodge Stratus cars for allegedly unsafe seatbelts. Chrysler claims the belts passed company-run tests prescribed by the agency, and says it's a victim of NHTSA's attempt to score points with consumers. "We get caught in the politicization of issues," gripes Chrysler spokesman Christopher Preuss.

Broadcasters are just as frustrated with the Federal Communications Commission, which wants at least three hours of educational kids' programming a week. "If indeed the era of Big Government is over, why hasn't the message gotten to the FCC chairman?" asks Edward O. Fritts, president of the National Association of Broadcasters.

The Clintonites' answer: Voters may say they don't like Big Government, but they do when it comes to protecting their health and safety. To the dismay of the GOP and its business allies, Bill Clinton has discovered that advocating a safer America is a safe issue with Americans.

By Catherine Yang

CAPITAL WRAPUP

RAISING FEARS TO RAISE FUNDS

► House Speaker Newt Gingrich of Georgia and Texas Senator Phil Gramm, two of the GOP's most formidable fund-raisers, are using a curious tactic to shake the money tree: They're crying wolf. While both enjoy large leads in their reelection races, their fund-raising letters warn that they're in big trouble. Gingrich claims his fight against cookie mogul Michael J. Coles is his "most difficult" ever. And Gramm begs for \$12 million for a "close and costly" race against cash-poor

Democrat Victor Morales, a teacher who has been driving around the Lone Star State in an old pickup.

JUST SAY NO TO BRIBERY

► The U.S. is stepping up pressure on Asian nations to clamp down on the bribes many businesses must pay government officials. When the Asia-Pacific Economic Cooperation summit convenes in Manila this fall, U.S. Trade Representative Charlene Barshefsky will push for an agreement to discourage the payoffs, which U.S. companies are barred from making.

PRACTICE, PRACTICE, PRACTICE

► Presidential candidates usually rehearse their nomination acceptance speeches shortly before their party conventions open. Not Republican Bob Dole. Aides are so terrified about his flat speaking style that they've given Dole a nearly finished speech more than a month before his Aug. 15 appearance at the GOP confab. And Dole already is practicing with a TelePrompTer. Still to be plugged into the text: details of an economic plan to slash tax rates and the budget deficit.

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SOCIAL ISSUES

PANGS OF CONSCIENCE

Sweatshops haunt U.S. consumers

Overnight, it seems, the use of cheap-labor factories in developing nations has sparked a First World debate. In the U.S., the issue is being politicized and Hollywood-ized in a distinctly American way. On July 16, talk-show host Kathie Lee Gifford—whose clothing line touched off the latest furor—shared top billing with Labor Secretary Robert B. Reich at a confab in Arlington, Va., where Wal-Mart Stores Inc. and Kmart Corp. announced new codes for overseas contract labor.

Why the outcry now? Credit the rapid globalization linking manufacturers, investors, and consumers everywhere. Increasingly, consumers can see how their shirts and sneakers actually are made, peering into the Indonesian factories where Nike will produce 70 million pairs of shoes this year and the Honduran maquiladoras that spawned Kathie Lee's dustup. *BUSINESS WEEK* correspondents visited these two countries to assess conditions.

INDONESIA

'ON THE INSIDE, IT'S HELL'

Despite improvements, Nike workers face tough conditions

The Nikomas Gemilang factory in Serang, 50 miles west of Jakarta, isn't owned by Nike itself, but it produces 1.2 million pairs of Nike sneakers every month. Like footwear factories everywhere in Asia, conditions are tough. Overtime is mandatory. Workers say exhausted colleagues regularly faint from overwork. Punishment for misdeeds consists of petty humiliation. A supervisor who skipped work one Sunday to care for his sick wife and child was forced to clean toilets and then was demoted. Another worker had to run laps around the factory because shoes she assembled had defects. "From the outside, Nikomas looks like heaven, but for workers on the inside, it's hell," says Sumantri, a 25-year-old activist who like many Indonesians uses one name.

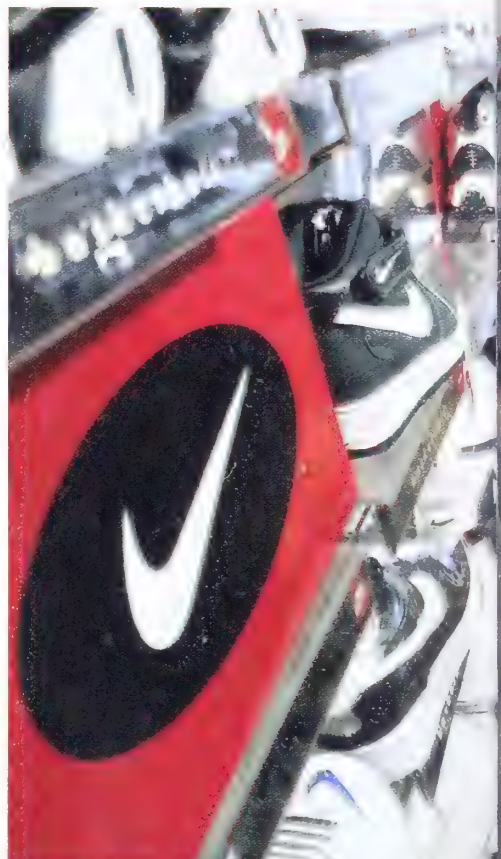
The marketing pizzazz of Nike Inc.'s "Just Do It" U.S. campaign is nowhere evident in the 12 Indonesian factories run by the company's Taiwanese, South Korean, and Indonesian subcontractors. Although these are some of the most modern factories in the industry, they are drab and utilitarian. Vast sheds house row upon row of mostly young women, who will glue, stitch, press, and box 70 million pairs of Nikes this year. Here, a pair of Pegasus running shoes, which retails for \$75, costs just \$18.25 to put together and ship to the U.S. Indonesia's military police deal harshly with those who rebel, and independent unions are outlawed.

LIGHTNING ROD. The stark contrast between the tens of millions of dollars that Nike icon Michael Jordan earns and the \$2.23 basic daily wage in Indonesia paid by the company's subcontractors has helped make Nike a lightning rod for concern about overseas manufacturing standards. Although Nike claims it's a leader in improving conditions, its Indonesian subcontractors secured an exemption from a minimum-wage increase that would have forced them to pay \$8.92 a month extra to each worker at a time when Nike has reported record profits.

More damning, say critics, is Nike's refusal to allow independent monitoring of its factories. Nike Chief Executive Philip H. Knight defends the Indonesian operations, saying that sneaker assemblers in Indonesia earn an average of double the minimum wage. But that because they have no choice but to work overtime. As for how subcontractors treat the workers, Knight says, "There are some things we can control and some things we can't control."

To its credit, the Beaverton (Ore.) sneaker giant, under intensifying scrutiny from U.S. labor groups, has done much to clean up more egregious violations, such as underpayment of wages that prompted workers at one factory to strike in 1994. No more do Taiwanese or Korean managers hit or verbally abuse local workers. "It's a different ball game today," says Tony Nava, a 16-year Nike veteran. Indeed, union activists at Nikomas say that a security guard who hit a worker in May was quickly fired.

Nike says it's setting high standards for others to follow in Asia, and cites as evidence the low turnover of workers at places like Feng Tay Indonesian Enterprises, a quiet, well-ventilated \$45 million factory near the center



CRUEL SHOES? New York shoppers like



Nike says it does what it can to keep the military police out of its factories. That's tough in Indonesia, where police help keep workers under control

but they may not be comfortable knowing the abuses workers endure

va city of Bandung, where a Taiwanese subcontractor manufactures shoes. At Feng Tay, every building plays a speech in English, Chinese, and Bahasa Indonesia promising that workers won't have to pay anyone to get a job at the factory and forbidding managers from withholding pay.

Even some critics give Nike credit. Muchtar Pakpahan, Indonesia's most prominent labor activist, says that the company's Nasa facility is "the best factory that I've ever visited." After an audit by Ernst & Young, ordered by Nike last year, subcontractors now are keener

on ensuring that workers wear protective gloves and masks and that fire extinguishers are properly maintained. Still, Nike has a long way to go before it lives up to its stated goal of providing a fair environment for all. Nike says it warns workers before they are fired that overtime is compulsory. But

Fitri, a 19-year-old junior high school graduate from Sumatra who paid a job broker nearly a month's basic wages to get her job at Nikomas, says she was told work finished at 3 p.m. when she applied. Instead, she regularly must stay until 9 p.m. or later. Only one worker out of more than a dozen interviewed at

Nikomas had ever heard of Nike's code of conduct.

There is also a not-so-subtle relationship between the managers of the factories and police, who help keep workers under control. This reporter got a taste of that power, and of the government's nervousness about the country's burgeoning labor movement, after a series of interviews set up by Pakpahan's union in

Serang. Eighteen plainclothes police detained me, along with three union members and an interpreter, for almost four hours, demanding an explanation of what I was doing. Two questions during my interrogation betrayed the regime's anxiety: What did the workers say about their conditions? Did I think the

minimum wage was high enough? Union activists say it's typical of the chronic harassment they endure.

Nike says it does what it can to keep police, a branch of the armed forces, out of its factories. But that's virtually impossible in Indonesia. After Muchtar Pakpahan visited the sprawling Nasa factory, at the invitation of management, he says the authorities forced the factory to fire three of his union's members and banned further contact with his group. "Employers cannot avoid a relation with the military, because it is the real power here," says human rights lawyer Teten Masduki, an attorney at the Indonesian Legal Aid Foundation.

Nike concedes its shortcomings in this arena. "We're dealing with governments that are less than ideal," Knight says. Although Nike's image is that of an on-the-edge rebel that likes to tweak authority, it has not challenged the Indonesian government's control over labor. As rumblings from workers grow louder, Nike would do well to be as much of a trendsetter in labor as it is in footwear fashion.

By Mark L. Clifford in Serang, with Michael Shari in Jakarta and Linda Himmelstein in San Francisco

HOW NIKE'S PAY STACKS UP



HONDURAS

CLEANUP AT THE MAQUILADORA

When U.S. clients complain, sweatshops make changes

ShinWon Honduras is cleaning up its washrooms. The South Korean clothing subcontractor in San Pedro Sula is buying fire extinguishers, installing emergency exits, and checking the ventilation—all in hopes of winning business from J.C. Penney Co. "Penney wants so many things," says manager Heung-Tae Kim. Meanwhile, other customers, among them Reebok International and Sears Roebuck, have laid down the law: No underage workers. So ShinWon has laid off 50 teenage girls.

Such is the fallout from TV personality Kathie Lee Gifford's tearful admission that clothes bearing her label were made under sweatshop conditions in Honduras. Most Hondurans have no idea who Gifford is, but some 74,000 people work in 200 *maquiladoras* clustered around San Pedro Sula, and many depend on U.S. apparel contracts. Since revelations of labor abuses surfaced in May, the Americans have tightened codes of conduct and stepped up the factory inspections. A Honduran government commission, U.S. human rights groups, and unions now sweep weekly through the city.

UNIONS BARRED. The attention showered on Honduras may well be improving the lot of its people. "Things have gotten better over the past couple of years," says Israel Salinas, president of the Independent Federation of Honduran Workers. The government, for one, appears more likely to recognize local organizing efforts. And local contractors are scrambling to deliver on demands from their U.S. customers for improvements.

The question in Honduras is whether the pressure will stay strong—and how much improvement the workers will actually see. Maria Herrera sews 1,500 cuffs a day on cotton knit shirts, typically earning about \$20 a week to support her six children. Even the most

militant unions can't force her wages up much in a country where the official unemployment is 35% and where most workers boast no more than a sixth-grade education. Government inspectors are slow to respond to allegations of forced overtime and unjustified suspensions, and Labor Minister Cecilio Zavala suspects that many of the plants are still preventing workers from organizing.

Nor does the economic pressure from abroad guarantee higher wages. J.C. Penney, for instance, now pays \$5 for the same two-piece toddler's outfit it bought at \$5.75 four years ago (retail price: two for \$16, on sale), forcing its U.S. manufacturer to find subcontractors

from Honduras' impoverished coffee-growing areas. Most, too, have little education and aren't encouraged to acquire any: When Oneyda Judith Rivera Flores, 20, asked her supervisor at Galaxy Park for time off to attend night classes, she was asked why she would want to study and was told she was needed for overtime.

ABOVEBOARD? The buzz at San Pedro Sula is that *maquiladoras* in the well-groomed industrial parks developed by Juan M. Canahuati are much better places to work. No wonder: They're among the few factories in San Pedro Sula with air-conditioning. At Int'l Fashions, a plant run by a Canahuati associate in his Choloma park, workers paid by the piece to sew Levi's Dockers and Nike shoes average about \$5.40 a day, twice the minimum wage.

More U.S. companies are seeking out relationships with operations such as Canahuati's, looking for some assurance of consistent quality and above-board labor conditions. Most forbid farming out work to a factory they haven't inspected, although unions and monitoring groups say unauthorized subcontracting persists throughout Central America. The most progressive American importers—Levi's, Gap, and Reebok among them—maintain a regular presence at their contractors' sites, assessing both product quality and labor conditions. "Thirteen people came to check us from Levi's," says Roberto Palomo, a lawyer for Seolim, a joint Korean-Honduran venture that is attempting to pass muster to win a Levi's contract. "You can't fool these people."

Monitoring has its limitations, of course. Who's to know if a contractor cranks up the air-conditioning the day an inspector from Gap shows up? Other U.S. importers such as



HARD LABOR Typical pay runs \$20 a week

J.C. Penney, moreover, have done little to improve enforcement at their contractors, relying instead on quality-control inspectors who tend to be more concerned with buttonholes and delivery times than with fire exits. Despite the new flurry to fix sweatshops, plenty of holes remain in the system. Will Kathie Lee make a difference in the long run? Honduras is waiting.

Most Honduran *maquiladoras* are vast concrete-block sheds, with only fans to combat the heat that settles over the coastal plain by 8 a.m. Salsa and *ranchero* music blares all day, while hundreds of workers cut, stitch, and press apparel. Most are young women, often single mothers, usually migrants

J.C. Penney, moreover, have done little to improve enforcement at their contractors, relying instead on quality-control inspectors who tend to be more concerned with buttonholes and delivery times than with fire exits. Despite the new flurry to fix sweatshops, plenty of holes remain in the system. Will Kathie Lee make a difference in the long run? Honduras is waiting.

By Elisabeth Malkin
in San Pedro Sula



SOUTH KOREA

SAMSUNG: NOT JUST THE CHIPS ARE DOWN

As semiconductor decline stalls expansion in other areas

Used to having their factories running seven days a week, three shifts a day, the 50,000 factory workers of Samsung Electronics Co. (SEC) are getting an unexpected opportunity to relax this summer. Since June, they've had two extra days off a month. They'll even get a paid five-day holiday, the first since 1992. They owe their break not to management but to the worldwide slump in memory-chip prices that has forced the world's largest maker to cut back production.

While exhausted workers rejoice, managers at other companies within giant Samsung group are worrying. Samsung's thriving chipmaking company has helped subsidize other parts of the group, South Korea's second-largest *chaebol*, or conglomerate. Now, with 1996 earnings set to slide by two-thirds, to some \$980 million, Samsung companies in autos, shipbuilding, and chemicals are having to slow their expansion efforts. "Plans were a bit too ambitious," says one Samsung insider, who says that lower profits will force the group to slash investments in marginal sectors.

LEE'S DREAM. Hard hit will be Samsung Motors Inc., the pet project of Samsung chairman Lee Kun-Hee. A car lover, he raised eyebrows last year with his plans to spend \$5.4 billion by 2000 to

create a new company able to build 500,000 passenger cars a year. That would turn up the heat on Hyundai, Daewoo, and Kia Motors and unleash a torrent of new Korean-made cars competing in international markets.

This year's car financing plan calls for \$2.3 billion, but that amount is now at risk. If Lee insists on maintaining that rate of investment, insiders say, the company may have to drop its existing business in trucks and buses. "If the worst comes, the group will have to give up the commercial vehicles," says a Samsung executive who declined to be identified. But the truck and bus business was only a stepping stone to passenger cars. Says the Samsung executive: "Cars are [Lee's] dream and will survive at whatever cost."

Officially, sagging earnings at SEC should have no impact on other Samsung businesses, since Samsung maintains it does not cross-subsidize group members. In an attempt to curb the power of the *chaebol*, the government bars a group member from investing

THROTTLED?
Chairman Lee's pet carmaking company may be delayed

more than 25% of its net assets in a related group company.

But it's a thinly veiled secret that *chaebol* affiliates use

deep-pocketed sisters for short-term funds, often working through an intermediary such as a group-owned financial institution. It's legal since the borrower pays interest, albeit at a low rate.

The semiconductor company has emerged as an increasingly important cash cow for the Samsung group, with combined sales of \$84 billion in 1995. Last year, SEC's \$3.2 billion in earnings, mostly from memory chips, made up 84% of the group's overall net profits (chart). That has helped fund daily cash transactions averaging \$1.3 billion in and out of Samsung Group companies.

STILL A POWERHOUSE. Despite the expected decline in profits this year, SEC is unlikely to have major cash-flow problems thanks to a heavy depreciation schedule. But the pricing slump has forced the company to halt plans for a second line to make 16-megabit and 64-megabit dynamic random-access memory (DRAM) chips at a facility in Austin, Tex. Now, SEC plans to install only one line that will make 64-megabit DRAMS no sooner than the end of 1997. "We have maintained a long-term relationship with the world's major personal-computer makers," says Sul Hee-Soon, an executive director of Samsung Electronics, who oversees semiconductor sales. "We don't expect them to betray us."

Other group companies will be less fortunate. Samsung General Chemical's ambition to become one of the world's top 10 by investing some \$2.5 billion abroad is likely to be put on hold. And

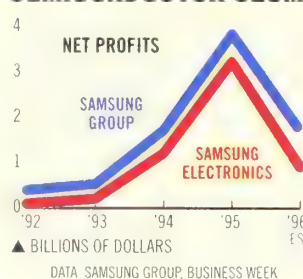
no money will be allocated to Samsung's ailing shipbuilding business, which is facing heightened competition from Japanese companies buoyed by the weaker yen.

Even as Samsung scales down its investments, the group as a whole will remain a powerhouse. Over the next five years, Samsung says that it will

spend 17% less than originally planned—which means it still plans to lay out an impressive \$63 billion. Some \$20 billion, or 31%, will go to semiconductors. Lee may still get a chance to rev up his auto engine, but for now, the chip downturn means he'll have to go a bit slower.

By Catherine Keumhyun Lee
in Seoul

SAMSUNG'S SEMICONDUCTOR SLUMP



FOR CEOs, THE BOUQUET OF BORDEAUX IS FADING

French companies are unloading their trophy vineyards



As a waiter fills guests' glasses with a luscious Bordeaux, André Lévy-Lang—hosting a lunch in his Paris executive dining room—smiles shyly. "It's one of ours," says the chairman of the management board at Compagnie Financière de Paribas. But lest lunch guests at his investment firm get the wrong idea, he quickly adds: "Our vineyards have been a very profitable investment." For Lévy-Lang, ownership of eight Bordeaux wineries is no ego trip.

The same can't be said for all French companies. For a decade, the fashionable acquisition for the company that has everything has been a Bordeaux chateau—better still, three or four. Banks and insurers, the biggest buyers, view them as real estate investments like any other. But critics consider "house wines" as little more than corporate trophies. For many French executives, "they symbolize success," says insurance analyst Jean-Baptiste Bellon of Deutsche Morgan Grenfell in Paris.

Now, France's morose economy has many CEOs wondering why they—or more likely, their predecessors—put scarce capital to toil in vineyards. At telecom giant Alcatel Alsthom, whose ex-CEO, Pierre Suard, bought Château Gruaud-Larose only two years ago, suc-

cessor Serge Tchuruk now plans to sell it along with another Bordeaux chateau.

Similarly, a new boss at investment firm Compagnie de Suez is paring down to a few core sectors and seems likely to put its seven vineyards on the block. "They're definitely not a strategic part of our business," says a Suez official. Insurer AGF may also dump its two Bordeaux chateaus. The company bought them in the mid-1980s simply because "it was the fashion of the moment," says an AGF executive.

The craze seemed to make sense. As world wine consumption grew, so did vineyard prices in Bordeaux, the region known for high-quality reds. Land in the Médoc that fetched \$9,000 a hectare in 1974 hit \$40,000 in 1984 and peaked at \$140,000 in 1993. Many families sold off vineyards when heirs needed cash to pay France's 40% inheritance tax. Buy-

"They're definitely not a strategic part of our business," says an exec at Suez, which may dump its seven wine chateaus

MEDOC VINES: Axa may keep properties like Pichon-Longueville-Baron

ers were often financial institutions that figured the market would keep bidding vineyard prices up. But bad harvests and weak economies since 1993 have led even Bordeaux real estate to plunge by up to 50%.

Corporate exits from vineyards delight traditional family vintners. "Companies just want to increase production to boost their returns," claims Jean Hugel, head of Hugel & Fils, an Alsatian producer. "The wines are never the same again." Hugel and colleagues have formed a global association of 12 big family vineyards, *Primum Familiae Vinea*. Members include California's Robert Mondavi. In France, the group is lobbying for relief from the inheritance tax, so families are not forced to sell.

PAYING RETAIL. In fairness, institutions are modest players, producing less than 5% of Bordeaux's output. And some have brought value to the vines. Paribas rebuilt the wine cellars at Mestrezat Domaines, a Bordeaux property bought in 1986. One day, it hopes to take the reborn winery public—a first for France. Having begun buying vineyards in the 1970s, when prices were low, Paribas gets an average 15% return on its investment. "That's not such a dumb business for a financial institution," says Jean-Paul Sabet, who manages the wine portfolio at Paribas.

Insurer Axa has also prospered. It rivals Paribas as the biggest institution investor in Bordeaux wineries, with mostly profitable holdings, including Château Pichon-Longueville-Baron, that are worth a total of \$200 million. Axa building conference centers at two vineyards—with 100 bedrooms—where it will train employees from its global empire, including Equitable Life Assurance. Critics call Bordeaux a playground for Axa wine-loving CEO, Claude Bébéar. But Jean-Michel Cazes, a veteran vintner who runs Axa's wine unit, says Axa has a deep commitment to wine and may buy some of the vineyards that its disillusioned rivals now want to sell.

Such sell-offs won't help morale in vineyard-owning companies. Most of them give discounts to employees on house wines, at least once a year. "That has been very popular here," says a spokesman at Alcatel. Paying retail may come as a shock. Yet Alcatel employees might consider lifting a glass to the new CEO anyway, for dumping a rather pointless investment.

By Stewart Taylor
in Paris

EDITED BY STANLEY REED

WILL HASHIMOTO LEAD THE LDP BACK TO THE GOOD OLD DAYS?

Japanese politicians call Ryutaro Hashimoto "Mr. Pomado" because of his fondness for thick hair gel. The Prime Minister has certainly turned in a slick performance since taking office in January. He has managed to shrug off the fallout from an unpopular thrift bailout to emerge as potentially the most powerful Prime Minister of the decade.

Hashimoto, 59, is getting a lift from Japan's strong economic recovery after four years of recession. He has also won praise for defusing tensions with South Korea over Japan's wartime transgressions and for cooling off trade friction with Washington without making big concessions.

SING TENSIONS. With his clout growing, Hashimoto seems closer to his aim of uncontested power for the Liberal Democratic Party, which now governs through a cynical alliance with the leftist Social-Democrats. Although he is required to face voters until mid-1997, many think Hashimoto is now confident enough to call a snap election for the 500-member Diet. "I'd bet on this year," possibly November, former LDP Prime Minister Kiichi Miyazawa predicts.

Hashimoto and President Clinton are acting like buddies, downplaying bilateral tensions during the political season. But once Hashimoto secures his power base, he could become more assertive. For example, he is pushing for China to get speedy admission to the World Trade Organization—something Washington opposes. A triumphant LDP is also most unlikely to enact the sort of sweeping deregulation the U.S. has long urged. And as the LDP reasserts power, the cozy old ways of money politics could come roaring back. Hashimoto's surprising strength owes much to the near-collapse of the opposition New Frontier Party, an alliance led by former LDP kingpin Ichiro Ozawa. Back in 1993, Ozawa helped lead a mass defection of LDP members that brought down Miyazawa's government, ending a 38-year party reign.



HASHIMOTO: Slick leader

But Ozawa's quest to reform Japan's grubby money politics and create a viable two-party system has failed miserably.

The Achilles' heel of Ozawa and his comrades has always been their own tainted backgrounds. Before casting himself as a crusading rebel, Ozawa was a legendary LDP power broker and fund-raiser. So it has been difficult for him to convincingly claim the moral high ground. His effort last winter to embarrass the LDP over its support of a \$6 billion bailout of corrupt thrifts failed when New Frontier members as well as LDP luminaries were shown to have taken loans from these institutions.

Ozawa's high-handed leadership has also alienated two key allies, former Premiers Tsutomu Hata and Morihiro Hosokawa. A New Frontier insider concedes that Hata and his roughly 70 followers have been listening to overtures to rejoin the LDP. Ozawa seems to have scotched that possibility, at least for the moment, through a round of meetings with Hata and Hosokawa in early July. But the public is disgusted with the so-called reformers. New Frontier's approval rating is down to a slim 10%. It's even possible that Ozawa will have to slink back to the LDP to save his career.

None of this is to say that Hashimoto won't face further obstacles. His own 40% rating is nothing to brag about. The banking crisis is still a potential minefield. And he needs to keep the recovery going. To stoke the economic engine, he is likely to cook up a \$30 billion-plus supplementary budget in the fall. Much of that money will go to public works spending, pleasing the LDP's backers in the construction industry.

Such handouts will fan worries about a growing budget deficit, but Hashimoto seems to hold most of the cards. After a series of revolving-door prime ministers, he could have a long run in power.

By Brian Bremner in Tokyo

GLOBAL WRAPUP

CREMLIN POWER GAMES

President Boris Yeltsin's shaky health has heated up the battle to shape the postelection regime. Jockeying for power are Prime Minister Viktor Chernomyrdin and security czar Alexander Lebed. Although Yeltsin has retreated to a sanatorium outside Moscow, his political instincts still appear sharp enough to play the two rivals against each other.

On July 15, Yeltsin strengthened Chernomyrdin's hand when he made the Prime Minister's ally, Anatoly B.

Chubais, presidential chief of staff. It was Chubais who masterminded Yeltsin's election campaign and many of the reforms of the past four years. Chubais will now control access to the president.

But Yeltsin also boosted Lebed by going along with his candidate, Igor Rodionov, for the key post of Defense Minister. Chernomyrdin had wanted to exclude Lebed from the cabinet selection process.

So far, the postelection moves have been a plus for business. During his talks with visiting Vice-President Al

Gore, Chernomyrdin agreed to cut taxes paid by foreign oil ventures. Executives are also pleased to see Chubais replace the hawkish Nikolai Yegorov, who was allied with anti-market figures.

American investment banker Boris Jordan, a kingpin in Russian finance, has already benefited from the change. He had been denied a visa, apparently because of his efforts to get rid of old-style managers at a steel plant. But his visa came through a few days after the election.

By Patricia Kranz in Moscow

THERE IS A PART OF YOU THAT REMEMBERS
(VAGUELY)

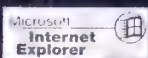
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WAYS TO GET THE JOB DONE.

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INSTRUMENTS**

WALL STREET'S DR. NO

Ex-Drexelite Leon Black is waiting for the stock market to tank

When Drexel Burnham Lambert Inc. collapsed in 1990 amid admissions of widespread securities fraud, the career prospects of Drexel investment banker Leon D. Black did not seem particularly auspicious. Much of the fraud related to Drexel's deals, and as head of the firm's mergers-and-acquisitions operation, Black worked closely

with Michael L. Milken, who went on to serve 22 months in prison.

Black emerged with a clean record, and now, six years later at age 45, he runs one of the largest and most successful private buyout firms, Apollo Advisors LP. Black's \$7 billion-plus empire consists of controlling or minority stakes in 26 diverse companies from coast to coast, including luggage maker Samsonite Corp. and Empire Kosher Poultry Inc.



Apollo's World



Arrowhead golf course near Vail, Colo.

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MINORITY STAKES

PACKAGING RESOURCE
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UNITED AUTO GROUP
UNITED INT'L HOLDINGS
LA SALLE RE
FOAMEX INT'L
PEPSI BOTTLING/S. AFRICA

Leaky gel in Converse sneakers was one slipup

His personal fortune is estimated at upwards of \$500 million. Apollo's net annual returns of about 40% dwarf the 29% and 24% returns posted as of Mar. 31 for buyout funds formed in 1990 and 1992, respectively, according to Venture Economics, a Boston research firm.

Although Black has striven to put a lot of distance between himself and Drexel, his dealmaking methods remain quite similar to those that made Drexel so successful during its heyday: finding outsize profits in adversity and misfortune. It was Drexel, of course, that pioneered dealings in so-called distressed companies and securities, especially junk bonds. This fall, Apollo expects to take possession of two choice midtown Manhattan office buildings it wrested from the collapsed Olympia & York Developments Ltd. real estate empire. That will essentially bring to a close one of the longest, largest, and most tangled financial restructurings in recent history. One banker thinks Apollo will double its \$100 million investment over a two-year period. No deal better illustrates Black's guile and readiness to plow big bucks—including his personal funds—into complex, dicey, troubled transactions.

Black, who has put \$7.5 billion to work in the past five years, expects that in the months and years ahead, Apollo will have plenty of opportunities to employ his \$1.5 billion war chest in similar sit-

uations. He raised the money from investors that included CalPERS, General Motors Corp.'s pension fund, foundations, and banks, exceeding Apollo's original target by \$500 million. In keeping with the firm's practice of placing its own net worth at risk, about \$100 million, or 7.5%, is the partners' money.

Black has believed for some time that equity valuations are excessively lofty and that the stock market will sharply reverse itself, creating plenty of distressed opportunities. "The only thing I'm sure of is that markets will change," he says. The market's recent sharp sell-off (page 24) suggests that these opportunities could emerge sooner rather than later.

"BLOOD." Black's view is echoed by other buyout artists, including Carl C. Icahn, Black's former client and erstwhile rival. Another is John H. Kissick, the former Drexel West Coast corporate-finance chief who works with Black and manages \$500 million in junk debt for Crédit Lyonnais and other investors. At the first sign of a major market reversal, Kissick says, Apollo is prepared to snap up bargains, much as it did when the junk market crashed in the early 1990s. The firm has tagged about 60 vulnerable companies it would consider acquiring once the market breaks. "Our sense is that in the next downturn, there could be some blood," says Kissick.

In its approach to the market—as well as its roster of former Drexel executives as Apollo officers and its close ties

With its \$1.5 billion war chest, Apollo is ready to snap up bargains

STRESSED

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LEMUNDO GROUP
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salant

Orders for slacks are on a slow mend

A taping of Telemundo soap opera Guadalupe

REAL ESTATE

O&Y BUILDINGS
DELANO HOTEL
CROCKER REALTY
WINTHROP FIN'L
CAPREIT

HIGH YIELD

\$500 million in high-yield bond positions, mostly rated B and BB



Black thinks real estate is one of the few sunny spots

publishing for \$150 million—a price some experts consider outrageously high—to an investor group led by Boston Ventures Management Inc. In June, Apollo agreed to sell its Crocker Realty Trust c. for \$540 million, generating an annual return of approximately 50%.

Apollo now views real estate as one of a few promising buying opportunities and is scouring the country for undervalued properties, including tax-sheltered limited partnerships and REITs. To that end, it expects to close this fall on a second \$500 million real estate investment fund; the first one posted an annual return on equity of about 50%. William Mack, head of Apollo's real estate unit, says office buildings and hotels are now selling for 45% to 75% of replacement cost. "There's not a lot of cash in real estate, so this is the best time to invest," he says. "Money is made when the market is improving and the reception is negative." The real estate market should continue upward for five more years, says Mack, a neighbor of Black's, whose son also works for Apollo. Notwithstanding the slow pace of non-al estate activity, Black says he expects to be out raising fresh capital for a new fund of the same size three years

from now. To keep Apollo's hand in the capital markets, the firm plans to start a high-yield fund. "We'll be making more [minority] investments as liquidity tightens, more control investments as the stock market falls, and more distressed as the economy weakens," he predicts.

AT ODDS. Black's reputation as a sharp-elbowed dealmaker is somewhat at odds with the one he projected growing up as the son of the late Eli Black. A rabbi turned socially conscious businessman, the elder Black rose to become chairman of United Brands Co. but committed suicide in February, 1975, by jumping from his 44th-floor window in what is now the Met Life Building in mid-Manhattan. Understandably, that had a profound impact on Leon, and he stiffens at the mention of it.

Early on, Leon's instincts, like his father's, seemed more those of a scholar and humanist than a businessman. A philosophy major at Dartmouth College, Black was passionate about basketball and Shakespeare and once wrote a 17-page essay on *King Lear's* fool. Black considered becoming a teacher, but his

father urged him to go to business school. He later received an MBA from Harvard, which he loathed. "Most of what I learned about how to do business I learned from Shakespeare, not Harvard business school," he says. Recently, Black endowed a chair at his

Some bankers say Apollo's success springs partly from his knowledge of ex-Drexel clients' holdings. Black's response: "Nonsense"

alma mater for Shakespeare studies.

Black was in his second year at Harvard when his father took his life. Eli Black's death didn't exactly leave his family penniless, but they surely were not rich even by 1970s standards. Leon wound up with a \$75,000 trust fund and an equal amount from a life insurance policy but promptly blew a third of it speculating on copper futures. From that, he learned to put his money only in places he understood. "I had to go out

and support myself and my family [his mother and sister]," says Black. He is now married, with four children. After his father's death, he wound up at what is now KPMG Peat Marwick and later worked at a publishing house. But it was a meeting with Frederick J. Joseph, then head of corporate finance at the third-tier investment firm of Drexel Burnham Lambert, that launched his dealmaking career.

As head of Drexel's fledgling cable-TV business in the late 1970s, Black made his mark by snaring Cablevision Systems Corp.'s chief, Charles F. Dolan, as a client and financing other cable ventures. In 1984, he underwrote John W. Kluge's buyout of Metromedia Co., one of Drexel's largest deals at that point. Two years later, he handled the sale of Metromedia's TV stations to Australian media mogul Rupert Murdoch. They formed the core of his TV network, Fox Broadcasting Co. Black acknowledges he did some ill-advised deals at Drexel. One was backing raider William Farley's ill-conceived takeover of bedding maker West-Point Pepperell, which landed Farley's company in bankruptcy. But former colleagues credit Black with being well ahead of the curve in betting on key

13, 1990
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cy protection

MARCH, 1992 Acquires \$3 billion junk-bond portfolio of defunct Executive Life Insurance, a major Drexel client

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Drexel Burnham
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Their Victim as Securities
It Holds Plunge in Value
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NEW YORK—Drexel Burnham Lam
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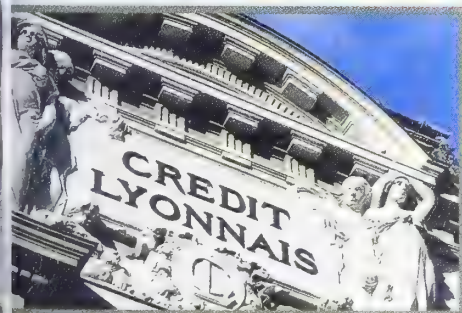
FALL, 1993 Apollo starts buying debt of Olympia & York (USA); expects to take possession of two prime Manhattan office buildings in late 1996

JULY, 1995 Finishes raising \$1.5 billion for Apollo III fund

JUNE, 1995 Completes acquisition of California chain Ralphs Grocery, last major buyout

APRIL, 1996 Announces sale for about \$540 million of its Crocker Realty Trust; to close in August

JUNE, 1996 Announces sale of 13.8% interest in Zale, a large jewelry chain; expects to close in late July



DATA: APOLLO ADVISORS LP, BUSINESS WEEK

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trends, such as cable in 1979 and leveraged buyouts in the early 1980s.

Of his 13 years at Drexel, the first 12 were "pretty terrific," says Black. There was a "fabulous feeling of camaraderie, esprit de corps." The last 12 months, however, were a "nightmare."

At the time, Black, like many of his Drexel colleagues, was angry at federal prosecutors, the financial press, and some "envious" members of the Wall Street Establishment, for, in his view, conspiring to undermine the high-flying firm and Milken, whom he still regards as one of the all-time geniuses of American finance. Black believes a lot of good came out of the junk-bond-fueled takeover wave of the 1980s. "Management was put on guard," he says. "And junk became established as a real market."

HEADSTART? Drexel's failure punctured the already deflated junk-bond balloon. Unable to obtain new financing, many Drexel clients stumbled. Suddenly, billions of dollars of distressed debt securities flooded the market, and no one was better positioned to evaluate their real worth than Leon Black & Co.

Much of the debt was issued by Drex-

el clients, in some cases Black's. The biggest deal was in 1992, the purchase of the \$3 billion (face amount) junk-bond portfolio of collapsed Executive Life Insurance, a California insurer and a Drexel client, with the help of Crédit Lyonnais, the large French bank. Even though Apollo outbid its nearest rival by a wide margin, the transaction remains emotionally charged. Critics such as Warren Hellman, general partner at the San Francisco investment firm Hellman & Friedman, who lost his bid for the portfolio, charge that Apollo capitalized on the naiveté of then-California Insurance Commissioner John Garamendi. "Nobody knew the portfolio better than Leon," says Hellman. "They helped create it." He adds: "What they were able to do is establish the ground rules and get the commissioner's office in a position where they were the favored bidder." Garamendi "made the worst deal of any grown person I've ever met in my career," says Hellman.

Some Wall Streeters claim Black was able to use his inside knowledge of ex-Drexel clients' holdings to turn fat profits buying and selling the junk debt of these

companies. "They had to have had headstart," says one. Black bristles at these charges, dismissing them as "nonsense." One Black defender, Wilbur Ross Jr., senior managing director of Rothschild Inc., says: "Five years is long time for inside information to have an effect." Since Black acquired the Executive Life portfolio at the bottom of the market, "it would have done well had he done nothing at all," Ross says. Black says his claimed 40% return excludes gains on the Executive Life portfolio.

In any case, Black, with his \$16.6 million bonus check from Drexel and \$8 million from Crédit Lyonnais and other mostly foreign, backers, was able to emerge from Drexel's ruins to found Apollo Advisors, named for the Greek god of sunlight, prophecy, and healing.

Drexel's failure had created an instant pool of skilled talent, and Black harp-picked the best of them. Top aides include Black's alter ego, John Hanna, second-in-command in the Drexel unit, Kissick, and Tony Ressler, Black's brother-in-law. Apollo quickly became known for its intellectual capital. Measured in sheer I. Q., Apollo's brainpower

DREXEL IS DEAD. LONG LIVE THE DREXEL NETWORK

Drexel Burnham Lambert Inc., the firm, is six feet under. But Drexel, the network, is alive and well. The firm's diaspora now permeates the upper reaches of the Wall Street Establishment.

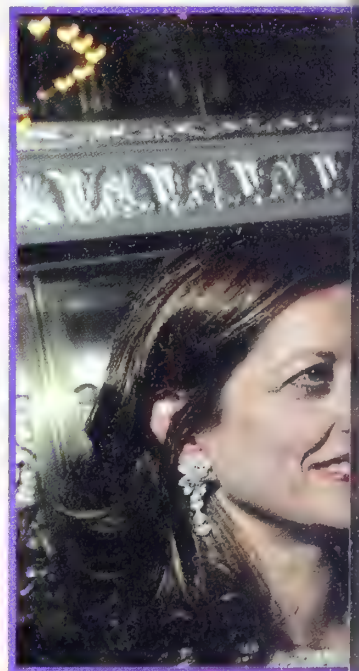
Just check out what, in many ways, is its Predators' Ball redux. The original soiree was the preeminent social event of a grandiose, bygone era in American finance in which Drexel and junk-bond king Michael R. Milken lavishly entertained their clients every spring at a posh Beverly Hills hotel. Now, the premier gathering of ex-Drexelites is the Lilac Ball, whose beneficiaries, befitting the times, are much needier than the L. A. version's were.

This year's party was held on June 3, seven years after Drexel threw its last bash at the Beverly Hilton. Leon D. Black, the driving force behind the current annual event, packed the Waldorf-Astoria's Grand Ballroom in New York with 1,300 friends and business associates. They paid an average of \$2,500 a person to honor him for his support of Prep for Prep, a charity that sends gifted inner-city youths to top private schools. The guest list read like a Who's

Who of 1980s dealmakers and big wheels from highly leveraged companies. Former Drexel Chairman Frederick H. Joseph was there. And MacAndrews & Forbes Group chief Ronald O. Perelman was a co-chair of the event.

SHARED LANGUAGE. For Black and Apollo, the ball is more than a well-spring of funds for a favorite charity. It's visible evidence of the network of high-powered investment bankers who, having survived their employer's demise, throw lucrative deals each other's way. The glue that holds the network together, however, is based less on friendship than on their shared language and credit culture, says card-carrying member Donald R. Mullen Jr., formerly junk-bond sales manager at Drexel's Beverly Hills office and now head of high-yield securities at Bear, Stearns & Co. Talking to an ex-Drexel banker means you don't have to waste hours explaining why a company with a good business plan but no cash flow should get financed, he says. During an early 1990s stint at another firm, Mullen

recalls, he and others tried to persuade colleagues lacking that background that lots of money could be made by injecting new capital into troubled corporations.



THE LILAC BALL: Black and wife Debra raising dollars for scholars, not raiders

daunting: Of its 30 professionals, about half, including Black, graduated at least magna cum laude from top universities. Meetings to deliberate over deals are typically loud, boisterous screaming matches. "The toughest thing at Apollo to finish a full sentence," says partner Marc J. Rowan, 34. Partners unwind by playing "old guys vs. young guys basketball."

Although Apollo's M.O. over the past six years has been shaped by the vagaries of the market, Black left Drexel with finite ideas about the kind of firm he wanted Apollo to be and where he planned to pick his targets. For one thing, he knew he didn't want to have to deal with the politics of a big firm. Good thing, says colleagues say managing a large firm is Black's weakest suit.

Black also ruled out hostile takeovers, saying they'd turn off prospective business partners. And he knew corporate raiders would avoid business with Apollo if it always held out for the last nickel. "[Black] may leave a nickel on the table. But no more than a nickel," says one Wall Streeter close to the firm. Apollo's strategy, Black says, is opportunistic yet long-term and risk-

averse: "If you cover your downside and keep the discipline, the reward side will take care of itself." Apollo is also unusually loose in its approach to deals. Unlike most other major buyout firms, which insist on acquiring control through equity investments in companies, Apollo

Unlike most other buyout firms, which insist on taking control through equity stakes, Apollo is flexible about the form of its investments and level of control

determined at the outset that it would be flexible in the kinds of investments it made in a company and in its willingness to share control. "Control is just one possible outcome," says Black. Apollo often invests with a view to getting control, but its fallback is an investment that will itself pay high returns.

The O&Y episode is a prime example of Apollo's ability to adapt to complex circumstances. Most prospective investors stayed clear, considering it a legal quagmire. One Apollo option was to take con-

trol of the entire U.S. operation. To gain leverage in the negotiations, Apollo persuaded bondholders and bankers to sell it their paper at an average of 50¢ on the dollar. Failing control, it knew it could end up with some of the buildings. At worst, it would earn a coupon on the bonds. Mack figured Apollo couldn't go wrong unless New York City was hit by a depression.

Apollo had to maneuver around a panorama of complex personalities and shifting alliances. From the beginning, two camps were clear. On the one hand, Canada's Bronfman family, banks—including Citibank, the largest lender to O&Y—and other creditors were seeking to minimize their losses.

On the other hand, Apollo hoped to make a profit by injecting new money. It did extensive due diligence—learning, for instance, that tenants of the buildings were happy with their leases, indicating that cash flow was reliable. Says Meyer "Sandy" Frucher, executive vice-president of O&Y (USA): "Everybody had the same opportunity they did. [But] no one else had the guts to do it."

In the end, the creditors, Apollo Advisors, the Bronfmans, and others agreed to divvy up the spoils, with

looked as us like we were Marjorie says. Among the financial institutions in the network members are prominent names such as Donaldson Lufkin & Jenrette, Bear Stearns, Bankers Trust Co. of the West. While launching Apollo, DLJ

snapped up eight of Drexel's top junk-bond experts and other specialists, including Kenneth Moelis, now DLJ's director of corporate finance. Overnight, DLJ leaped into the upper ranks of the creative-lending fraternity. "We do bridge deals for Apollo no one else could," says Moelis. "Because of our long relationship, we're willing to go the extra mile."

NO BLINKING. Take United International Holdings Inc., the cable company in which Apollo owns a 13% stake. In 1994, when UIH needed a \$50 million bridge loan to complete a European joint venture, Moelis didn't blink even though UIH had virtually no revenues. "We never felt it was risky," he says. "We put in the time to understand it." The loan was refinanced, and DLJ has since completed more than \$400 million in financings for UIH. Likewise, Apollo frequently calls on Mullen and others at Bear Stearns, an investor in Apollo funds, for restructuring advice and debt underwritings, such as last year's \$190 million debt issue for Samsonite Corp.

The Drexel connection also appears to have figured in

Bankers Trust's becoming Apollo's lead commercial bank. According to former Drexel high-yield debt trader Ted Virtue, now the bank's head of global finance, BT has invested with Apollo in its major supermarket deals and in its acquisition of Big Flower Press Inc., a newspaper-insert printer. And the bank typically gets the nod to arrange bank financing for acquisitions by Apollo companies, as it did in late 1995, when Furniture Brands International Inc. bought Thomasville Furniture Industries Inc.

When Apollo needs to place a junk bond or private debt placement for one of its companies, it invariably phones Trust Co. of the West's Mark L. Attanasio and Robert D. Beyer, both of whom once worked for Apollo partner John H. Kissick in Drexel's L.A. corporate-finance office. In 1994, says Attanasio, the relationship was put to the test briefly in 1994, when Apollo's Empire Kosher Poultry Inc. stumbled badly. Black installed new managers, who cut costs and bolstered marketing while continuing to pay interest on TCW's private debt placement. Today, TCW holds \$95 million in Apollo paper. "Leon's deals have an edge because he is a proven moneymaker," says Attanasio. While the network helps, money is always the best edge.

By Phillip L. Zweig in New York



Black loathed Harvard B-school: "Most of what I learned about how to do business I learned from Shakespeare, not Harvard"

Apollo getting 1290 Avenue of the Americas and 237 Park Avenue, O&Y USA's headquarters. Mack says he expects Apollo to hold on to the buildings for the "intermediate term."

Apollo chafes at being typecast as a distressed or "vulture" investor. But it was distressed-debt investments that got the company off and running in the restructuring business and that have produced the best returns. In 1990, says Ressler, Apollo recognized these investments as "real companies with real franchises. They weren't going away, even though people were saying high-yield bonds were bad." Adds Black: "One of the reasons we liked distressed was because others didn't have the capital-markets background and weren't comfortable playing" in that arena.

The transaction that marked Black's return to deal-making's center stage was Apollo's acquisition, beginning in 1990, of 40% of the senior subordinate debt of what was then Harcourt Brace Jovanovich, which overleveraged itself in 1987 to block a takeover attempt by British newspaper baron Robert Maxwell. Most prospective investors were frightened by junk bonds. But at a time when many companies were valued at about eight times cash flow, HBJ debt was only about 3.5 times its \$200 million cash flow. Black figured the investment was virtually risk-free. After he offered about \$1.2 billion in cash and notes for the company, Richard A. Smith, head of Boston-based General Cinema Corp., topped it by \$400 million with an all-cash bid. Ever flexible, Apollo was still able to cash out after nine months with a \$100 million profit.

GAME PLAN. Once Apollo takes over a distressed company, it usually follows a fairly predictable formula: It dumps marginal assets, replaces or motivates management with a package of incentives, recapitalizes the company, and takes it public. Take troubled E-II Holdings, formerly American Brands Inc. and later known as Astrum International Corp. Holdings included Culligan Water Technologies, the water-purification company,

and luggage maker Samsonite Corp. As has been his practice in perhaps 40% of Apollo's deals, Black acquired major positions in various debt tranches, which gave it a "blocking position," the ability to control the deal's outcome and eventually convert its interest into a big equity stake. Apollo in 1993 led senior debt holders in a prolonged, acri-

been in hot pursuit of closely related companies and are moving to expand their traditional businesses outside the U.S. It seems to have paid off: Culligan and Samsonite are trading for a combined \$51.50 a share, compared with Astrum's \$23 a share before restructuring.

For all of its due-diligence skills, Apollo has endured a few embarrassing, high-profile blunders. Its biggest headache is surely its Family Restaurants Inc. unit, a company it formed by merging its own troubled restaurant unit, which included the El Torito, Carrows, and Coco's chain, into Foodmaker's Chi-Chi's Mexican-style restaurant chain. Apollo appears to have been less than vigilant in overseeing the new operation. Maintenance and service had deteriorated dramatically even before July, 1994, when a report by a nutrition-advocacy group branded Mexican food as unhealthy. Foodmaker panicked, discarding traditional menus in favor of healthier selections that went over poorly with customers. Apollo declines comment on its opinion of Foodmaker. But in cleaning up the red ink on the kitchen floor, Apollo assumed Foodmaker's interest in Family Restaurants and installed new management. A Foodmaker spokeswoman said sales declined after the report.

Sneaker maker Converse Inc. has been another major disappointment. There, everything that could go wrong happened. Last May, for example, Converse bought sports-apparel maker Apex One Inc. but shut it down three months later, taking \$41.6 million pretax loss. Then, in December, Converse's "performance" sneakers leaked cushion fluid at the start of a high school basketball game in a Chicago suburb, causing the players to slip and slide across the court. "It's a tough business," shrugs Hannan. "They [Converse] have their work cut out for them."

Dealing in distressed situations, of course, is always tough. But if the market downturn Black anticipates occurs in his life, if not those of most of his competitors, should be a lot easier.

By Phillip L. Zweig, with bureaus reports



A GOOD DEAL: Black is still bullish on supermarkets

monious battle against junior debt holders, notably Carl Icahn. Eventually, Icahn made a bundle on the junior debt, while Apollo wound up with a controlling stake in the reorganized company.

After Apollo took over, it replaced Culligan's management, which it regarded as uninspired. And it fired up new management with a package of incentives, including stock options. Apollo proceeded to sell off a T-shirt maker and a meatpacking company, whittling Astrum down to Samsonite and Culligan, which it spun off in August, 1995. Apollo is the largest shareholder of the two companies. Lately, Culligan and Samsonite have

BY GENE G. MARCIAL

SMALL-CAPS THAT EAT A FEATHER

The market sell-off slammed NASDAQ small-capitalization stocks hardest, but not everyone ducked for cover. Money manager Audrey Jones stood firm: "We stepped up buying of our favorite small-caps even as the crowd fled out," says Jones, who co-man-



JONES: Standing firm in the sell-off

ages the \$600 million small-cap and micro-cap portfolios at Morgan Grenfell Asset Management, a unit of Deutsche Bank's Morgan Grenfell Capital Management. Jones's chief buys during the deep slump: Atlantic Southeast Airlines (ASAI), homebuilder D.R. Horton (DHI), hardwood-floor maker Triangle Pacific (TRIP), and US Freightways (USFC). The market's pullback, says Jones, makes these stocks even more undervalued, given their sturdy fundamentals and upbeat earnings outlook.

Morgan Grenfell's small stocks, she notes, have outscored the Russell 2000 Small-Cap Index by quite a wide margin this year—through July 16.

Atlantic Southeast is "a play on the Olympic Games," says Jones. This regional carrier, with scheduled service to cities in 13 states from hubs in At-

lantic Southeast Airlines (ASAI), homebuilder D.R. Horton (DHI), hardwood-floor maker Triangle Pacific (TRIP), and US Freightways (USFC). The market's pullback, says Jones, makes these stocks even more undervalued, given their sturdy fundamentals and upbeat earnings outlook.

WHAT JONES KEEPS UP WITH

	STOCK PRICE	EST. 1996 EPS	1996 TARGET PRICE
ATLANTIC	24	\$2.00	\$30
D.R. HORTON	9	0.90	15
TRIANGLE	19	1.65	27
USFREIGHT	19	1.48	30

DATA: BLOOMBERG FINANCIAL MARKETS.
MORGAN GRENFELL ASSET MANAGEMENT

tanta and Dallas-Fort Worth, has been around since 1979 and benefits from ties with Delta Air Lines, which owns 25% of Atlantic. Its commuter service links up with Delta's long-haul flights. Jones sees Atlantic making \$2 a share in 1996 and \$2.25 in 1997, up from \$1.55 last year.

D.R. Horton, a builder of single-

family houses, was hurt by the rise in interest rates this year. But Jones expects it to do better in the second half, when she thinks rates will fall. She figures Horton will make 90¢ in 1996 and \$1.10 in 1997, vs. 1995's 74¢.

With 40% of the U.S. hardwood-floor market, Triangle Pacific has been on a roll: Its stock has risen from 15 in February to 19 on July 16. The outlook remains upbeat: While 47% of houses built in Japan and 20% in Europe have hardwood floors, only 2% in the U.S. are so equipped. "So Triangle has much more room to grow," says Jones. She sees earnings of \$1.65 in 1996 and \$2 in 1997, up from 1995's \$1.49.

US Freightways (formerly TNT Freightways) has been on the skids because of high fuel costs, stiff competition, and bad weather. It operates trucks on regional routes for shipments of less than 10,000 pounds. But Jones expects the stock to snap back as business picks up in the steady economy.

The carnage in small stocks, she believes, is over and forecasts that her picks will continue to outpace the pack.

READY TO COIN IT FROM PAY PHONES

A group led by investor Chuck Davidson of Wexford Partners Fund is betting that "smart" public phones will soon displace the country's 2.1 million existing pay phones. So it has taken a 52% stake in Technology Service Group (TSGI), a provider of pay-phone systems and services to the Baby Bells.

"Upgrading pay phones to micro-processor-based hardware and software represents a market of \$500 million to \$750 million over the next five years," says a money manager close to Wexford Partners. Some 10% of U.S. pay stations have already been converted to smart phones, he notes.

One smart feature lets callers use prepaid debit and credit cards. The technology also permits portable or wireless pay phones to be installed in buses, trains, or taxicabs. For the Baby Bells, smart phones will allow remote monitoring of the pay phones for efficient billing and servicing.

Technology Service already has links with the Baby Bells, principally Nynex, Bell Atlantic, and Southwestern Bell, which accounted for \$29 million, or 87%, of the company's sales in the year ended Mar. 31, 1996.

Coming up, says one money manag-

er, is a \$50 million contract Technology Service is expected to sign with a major Baby Bell to upgrade its phones. The company declined to comment on such a contract. One official who asked not to be identified says Technology Service will form alliances with one of the Baby Bells to install pay phones in Mexico, Venezuela, Brazil, and China.

Analyst Stuart Gauld of Brookehill Equities, which took Technology Service public on May 10 at 9 a share, says the company has a 30% to 40% share of the total upgrade business. He figures the stock, now at 10, is worth 20 based on his estimate of 40¢ a share for the year ending Mar. 31, 1997, and 65¢ for 1998.

A LASER FACELIFT FOR EQUIMED

Cosmetic laser surgery, anyone? EquiMed (EQMD) expects to be able to provide such a service this year. Within a week, the company expects to sign an agreement, says one investment manager, with Palomar Medical Technologies to establish laser centers at all EquiMed clinics.

EquiMed owns or operates 30 radiation oncology therapy centers and 18 ophthalmology clinics in 16 states. These include seven ambulatory surgical units.

Palomar makes lasers, used mainly for burns, cosmetic dermatology, and hair removal. Palomar's EpiLaser won a Food & Drug Administration O.K. in July for dermatological applications.

By next year, EquiMed and Palomar expect to have set up 50 to 60 laser centers around the country. Each center, estimates one analyst, could bring in yearly revenues of \$2 million, for a total of \$100 million. EquiMed and Palomar will split sales and earnings equally.

Analyst Craig Dickson of Everen Securities projects that, even before any contribution from laser centers, EquiMed will earn 45¢ this year and 85¢ next, vs. 31¢ in 1995. Now at 7, EquiMed is worth 20, figures Dickson.

WILL SURGERY STOP THE SAG?



DATA: BLOOMBERG FINANCIAL MARKETS

EDITED BY PETER COY

PHONES JUST GET SMALLER AND SMALLER...

CELLULAR PHONES ARE getting so small you can't cradle them on your shoulder without inviting a trip to the chiropractor. Two companies are doing something about that.

In a bow to Dick Tracy, Japan's Nippon Telegraph & Telephone Corp. has developed a prototype phone that fits into a wristwatch weighing just 2½ ounces (photo). There's no touch pad, because a user dials by speaking. The lithium-ion battery and antenna are in the watchband. NTT researchers hope to develop batteries by early 1998 that

will make the phone powerful enough to work with Japan's digital cellular service, the personal handy-phone system.

But as Dick Tracy knows, speaking into a wristwatch ties up your arm. Aura Communications Inc., a year-old Wilmington (Mass.) startup, solves that by breaking a phone into two parts. One part fits in the ear and has a lightweight arm extending to the mouth. The other



infrared or radio waves, the two parts communicate by inducing magnetic fields in each other. This consumes little power at short range, so one rechargeable button cell gives the ear-piece at least eight hours' use.

Aura says its patented magnetic-induction system could be used with other phones, including cordless sets for home and office. It's selling its technology to phone makers. The first systems should go on sale early next year, says President Frank A. Waldman.

Steven V. Brull

A MOLECULE THAT MOPS UP WATER IMPURITIES

DUTCH CHEMISTS HAVE COME up with a molecule that gloms onto and removes tiny bits of impurities in water—from gold to radioactive waste.

The molecule is an advance over existing water-purification systems, many of which work on the principle of ion exchange. Impurities in a solution break down

into positively and negatively charged ions. Ion-exchange systems remove only one set of the ions, either the positive ones, such as calcium or cesium, or the negative ones, such as chlorides or phosphates.

The Dutch molecule—which is incorporated into a filtration membrane—gets rid of both positively and negatively charged ions, says team leader David N. Reinholdt, head of the department of supramolecular chemistry and technology at

the University of Twente in Enschede.

The molecule operates in two stages. First, it draws the positive ions to one end. The capture of those substances changes the other end of the molecule so it can capture the negative ions that remain. Also, it can be tailored to grab specific ions, even in tiny amounts that other processes miss. A Dutch company Reinholdt declines to name has right of first refusal on the molecular trap. □

CAN TREE 'BOMBS' FIGHT GLOBAL WARMING?

LOOK OUT BELOW! TREES being planted by airplane! If that sounds like a joke, you haven't been talking to Moshe Alamaro. The doctoral candidate in mechanical engineering at Massachusetts Institute of Technology proposes to reforest large expanses of the planet by air-dropping billions of young trees in remote areas where ordinary planting is impractical.

His goal: To help stave off global warming, since trees capture carbon dioxide from the atmosphere.

The trees—when they are 6 to 12 inches tall—would be placed in spearlike containers that would pierce the soil, then degrade. Velocity on impact: 120 to 150 mph. Alamaro and a fellow MIT PhD candidate, Nicholas Patrick, hope to assemble an international consortium, in-

cluding a company that would provide an airship to scout locations and ensure no one is in the target zone.

Backers might include utilities that could earn pollution credits by helping soak up carbon dioxide.

Forest-products companies tried to be aerial John-

ny Appleseeds 25 years ago, but too few of the trees took root and grew, says Donald P. Hanley, an extension-ser-

vice forester at

Washington

State Universi-

ty. Alamaro

hopes to build

on those ex-

periments by

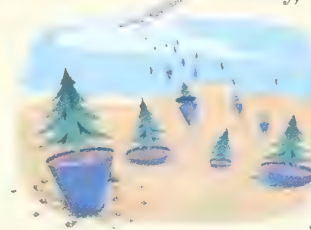
using a more

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tainer that will pierce deep-

er and by being choosier

about where to drop trees. □



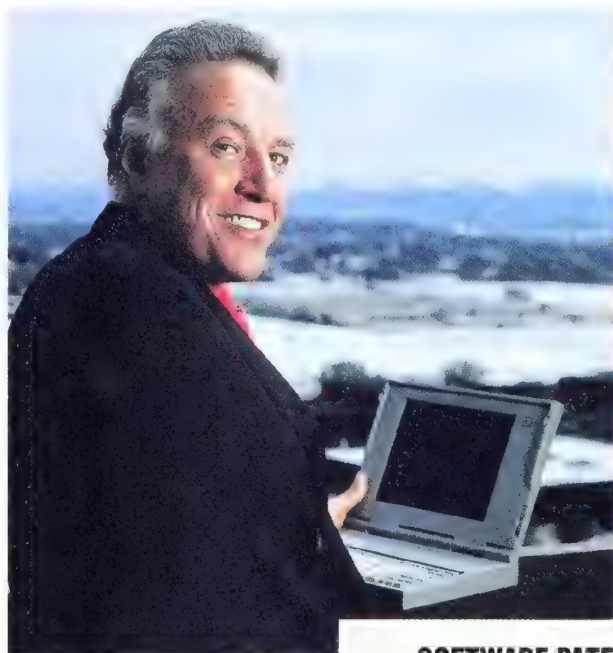
PATENTS

E-COMMERCE: WHO OWNS THE RIGHTS?

E-data's patent claims are causing an outcry—and raising fears of an icy way full of roadblocks

David S. Rose got a nasty surprise last month when he opened a thick envelope from E-data Corp. in Secaucus, N.J. Rose, chairman and CEO of a New York Internet-software startup, Ex Machina Inc., was told that his company might be infringing E-data's patent on electronic commerce. He knew from earlier press reports that E-data had sued a dozen other companies over similar claims, so he took the threat seriously. E-data was making a bold attack, saying it was due royalties on a broad range of online transactions. The patent, if valid, could cost E-data millions of dollars, Rose realized. And if other patent holders followed E-data's example, a wave of aggressive patent enforcement could stifle commercial activity on the Net. But as Rose studied E-data's patent, nothing about the terrain it covered seemed disturbingly familiar. "I'm not a lawyer," Rose says, chuckling, "but how do you get a patent on something that already exists?"

OPER REVIEW? Rose quickly determined that the patent didn't apply to his company, but he had news for the lawyers wrangling with E-data's claims. He remembered a small startup called Telephone Software Connection in Torrance, Calif., which let users of Apple II computers—including Rose—download programs automatically over telephone lines. The idea was supposed to be covered by E-data's patent. But Telephone Software, which is no longer in business, was doing it in 1980—three years before E-data's patent was filed. If a patent's claims cover technology that existed previously, a judge can render it invalid. Today, as the Internet expands by leaps and bounds, E-data's claims strike



many experts as both obvious and overly broad. They fear that many more patents like it may be lurking—unexploited—in the portfolios of giant companies that collect software patents like shells on a beach. That's one reason E-data's legal battle has riveted the attention of software and patent experts across America and spawned discussion groups on the World Wide Web.

A central question is whether E-data's application received proper review by the patent office. U.S. District Court Judge Barbara S. Jones will begin to dig for answers next month, when E-data lawyers explain in court how the activities of 14 software and publishing companies it has sued in-

fringe its patent. The defendants—who's who of software and publishing powerhouses, including CompuServe, Broderbund, Ziff-Davis, and The McGraw-Hill Companies (owner of BUSINESS WEEK)—will argue that E-data's patent echoes ideas that were current in the marketplace prior to 1983. That was their legal strategy even before Rose made the link with Telephone Software Connection. Rose simply gave the publishers' lawyers more ammunition.

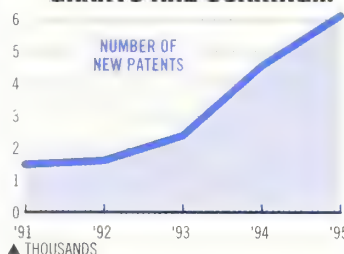
FREILICH: *His methods have irked many* If the patent office had searched more widely, it would

have found numerous press write-ups on Telephone Software Connection, founded by entrepreneur Ed Magnin in 1979. In 1980, for example, *Popular Mechanics* went so far as to predict that Magnin could be "the first in a long line of industrious computer-age merchants." Magnin himself is eager to tell his story. "E-data is trying to stifle electronic commerce," he says. "I don't think the government is going to let them."

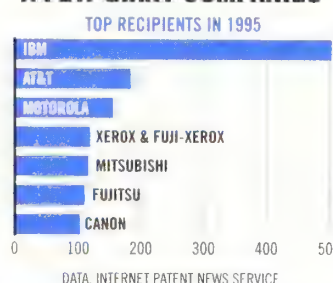
Even critics of E-data's patent, however, respect its author's intelligence and energy. In 1983, in 36 pages of painstaking detail, inventor Charles C. Freeny Jr. sketched out his idea for a network of "information manufacturing machines" that could swap encrypted digital information over phone lines. The language of the patent defines this information as the content of "tapes, videodisks, handheld calculators, handheld electronic games, greeting cards, maps, and sheet music," and it also specifies digital payment schemes. Says Calvert D. Cray, a litigation analyst at securities firm Auerbach, Pollak & Richardson in Stamford, Conn.: "This guy definitely had an insight."

In 1989, Freeny sold the patent to an electronic distribution company called Avedas Inc. When that company foundered, the patent was bought by

SOFTWARE PATENT GRANTS ARE SOARING...



...AND MOST GO TO A FEW GIANT COMPANIES



another startup, Interactive Gift Express, which later changed its name to E-data and is now devoted exclusively to exploiting the Freeny patent.

The company is a lean, three-person operation run by retired investment banker Arnold Freilich. Convicted of stock fraud in 1978, Freilich was barred from stockbroking. But as CEO of E-data, he has racked up some early successes with the Freeny patent. In September, 1995, after months of negotiations, he persuaded IBM to sign a license. Freilich also struck a deal with graphics software giant Adobe Systems Inc. and others. IBM and Adobe say the agreements prohibit them from discussing the terms of their licenses. But information from E-data states that, in general, fees may range from a few thousand dollars up to \$40,000 a year.

Hardly a mortal burden. Still, Freilich's modus operandi has incensed many of the companies he has approached. E-data has sent out 25,000 glossy information packages containing copies of the Freeny patent, licensing forms, and other materials. Freilich dubs the mailings "amnesty packages," because they offer discounted licensing terms to companies who sign early—before they are sued. "We are not out to undermine the world, destroy the economy, or hurt small companies," says E-data lawyer and patent-litigation veteran David Fink. "We just want reasonable royalties."

CATCHING THE BUG. But patent attorney John P. Sumner of Merchant & Gould in Minneapolis calls the whole approach "flippant." Usually, he says "a patent holder has a clear idea that a company is infringing before it sends out notice."

Even if E-data's patent is overturned, as seems likely, disputes over software patents won't disappear. Some 20,000 software patents were granted in the early '90s, and more than 7,000 will be issued this year (chart, page 65), says Greg Aharonian, founder of Internet Patent News Service. Many, like the Freeny patent, get approved without due consideration of related technology, or "prior art," Aharonian charges.

Until recently, most software patents were held by huge hardware companies such as IBM, Motorola, and Fujitsu. But those companies often didn't exploit them. Now that's changing. IBM has begun to license its patents more aggressively. And software goliath Microsoft Corp. has caught the same bug. Half of the company's 140-odd patents were obtained in the last two years. Whatever the outcome of E-data's lawsuits, software patents have come of age: In the eyes of many managers, they are simply too valuable to leave unexploited.

By Neil Gross, with Amy Cortese, in New York

Information Processing

TELECOMMUNICATIONS

DID MOTOROLA MAKE THE WRONG CALL?

How it wound up in the back of the pack in PCS

If a company could use a hot-growth market right now, it's Motorola Inc. And it seems there's one at hand: Just as Motorola's semiconductor and cellular-phone businesses are in the doldrums, a new kind of wireless calling known as personal communications services (PCS) is on the horizon. The Federal Communications Commission has auctioned licenses to three PCS operators in each city across the U.S., and over the next five years, these operators will spend \$15 billion to \$23 billion building PCS networks, estimates market researcher Yankee Group Inc. It's a perfect opportunity for Motorola, a top supplier of cellular-network gear.

But Motorola has all but guaranteed itself a trailing position in the U.S. PCS market. Its share of the U.S. PCS-equipment market so far is only about 12%, well below its 20% share in conventional cellular transmission equipment, according to Yankee Group. "They don't have that many contracts," says Peter Nighswander, a senior consultant at Economic Management Consultants International. "It looks like Ericsson, Lucent, and Northern Telecom are beating them out."

PUZZLEMENT. How did Motorola get in this position? For starters, the company has continued to push a single technology for PCS in the U.S. rather than offering carriers a choice. Equally important, the company is reluctant to offer the kind of financing deals that the network builders have been asking for. That's why Motorola took itself out of the bidding for the biggest deal so far, a \$3 billion network being built by Sprint Corp. and a group of cable-TV operators. Lucent Technologies, the soon-to-be-independent AT&T equipment arm, and Northern Telecom teamed up and agreed to underwrite the cost of the contract, a common practice for huge telecom infrastructure projects.



FOR THE DEFENSE

"You have a limited amount of investments to make. We have to prioritize global opportunities," says Motorola's Finlayson

It's a puzzling state of affairs for a company that has long been the envy of Corporate America. For three years, the high-tech behemoth had shown that even a huge company, if managed correctly, can rack up impressive growth. Revenues grew an average of 27% annually, to \$27 billion in 1995, while net income surged 58% a year over the same period, to \$1.8 billion. "They were firing on all cylinders," says Ajay Diwan, analyst with Goldman, Sachs & Co.

On July 9, the growth machine of

ily stalled. After reporting second-quarter results 22% below what analysts were expecting, Motorola sent other high-tech stocks and the entire market into a tailspin. Worse, analysts warn that revenues will be flat for the year and profits will fall 15%. Vice-Chairman and CEO Gary L. Aaker placed much of the blame on circumstances beyond Motorola's control—specifically, slowing demand and a profit-killing price war in cellular phones and a downturn in chip sales. But a downturn in business cycles doesn't explain Motorola's missteps in PCS, where it has badly bobbled the chance to replace fading markets with a new one.

CDMA and offers only CDMA equipment in the U.S., even though about a quarter of the PCS operators plan to use GSM. "Strategically, they made a big mistake," says David Lasier, president of Telecom Wireless Solutions Inc., an Atlanta-based consulting firm. "Motorola should have positioned themselves to do both GSM and CDMA in the U.S."

Oddly, Motorola isn't anti-GSM overall, just GSM in the U.S. It gladly sells GSM equipment overseas. But lots of other companies sell GSM equipment as well, whereas Motorola is one of the few manufacturers licensed to push CDMA—which it hopes will give it a competitive advantage. "We're focusing on CDMA be-

parable CDMA parts. "We think we have a cost and availability advantage," says Don Warkentin, president and CEO of American Portable Telecom, which is building GSM systems in six U.S. cities and Guam.

Motorola is beginning to hedge its bet in the U.S. It plans to offer some GSM equipment in the U.S. in about a year, figuring it can pick up some add-on contracts from GSM operators that are expanding their networks. But that's a tough sell: It's difficult to displace rivals who get the initial PCS contracts. "If you're an incumbent supplier to a wireless operator, you're almost assured of the add-on business. It's like an annuity," says Marc Cabi, analyst at Salomon Brothers Inc.

As to its reluctance to finance PCS deals in the U.S., Motorola says it's making such investments overseas—in Asia and Latin America, where demand is even greater. "You have a limited amount of investments to make," says Finlayson. "We have to prioritize the global opportunities." He says it's smarter to pursue contracts in Brazil, for example, where 1 million people are on a waiting list for wireless telephone service—and only minimal financing is required.

RICHEST MARKET. Certainly, sales of wireless equipment outside the U.S. are booming. Already, 80% of the revenues for Motorola's wireless infrastructure group comes from overseas markets, where annual growth is 35%—twice the U.S. rate. Still, analysts say, Motorola can ill afford to let the world's richest market slip through its fingers. "If Motorola had the resources, they could have been more aggressive. Long term, there will be a return on these investments," says John Ledahl, a consultant for market researcher Dataquest Inc. So far, Motorola's only major PCS contracts are with GTE Mobilenet and PCS PrimeCo, a team of three Baby Bells and Air-Touch Communications.

Of course, Motorola's future does not hang on PCS alone. With innovative products such as the palm-size StartAC, Motorola is likely to keep its lead in cellular phones. The market for wireless phones is expected to more than double over the next five years, to 35.5 million units a year, according to Dataquest. Revenues will grow from \$6.25 billion this year to \$11.45 billion in 2000.

Paging, although relatively small, is growing rapidly as well. Hambrecht & Quist analyst Rakesh Sood estimates that Motorola's paging revenues will grow 20% to 25% annually for the next few years. Motorola's cable modems and two-way radio products also look promising.

The recovery path in Motorola's chip business isn't as clear. The unit, which

WHERE MOTOROLA MAKES ITS MONEY

WIRELESS PRODUCTS

SALES: \$10.66 billion

OPERATING PROFITS: \$1.27 billion

ISSUES: Prices of cell phones are falling while demand is slowing. Because of internal decisions, Motorola is losing sales of gear for personal communications services in the U.S.—a huge growth market.

PAGING AND MODEM PRODUCTS

SALES: \$3.68 billion

OPERATING PROFITS: \$310 million

ISSUES: Paging business is growing rapidly because of Motorola-backed standards and innovative products. Modem pricing is soft.

SEMICONDUCTOR PRODUCTS

SALES: \$8.34 billion

OPERATING PROFITS: \$1.22 billion

ISSUES: After several boom years, industry growth is slowing. Motorola is particularly exposed to problems at Apple, though sales of controller chips (for autos and other products) are still growing.

LAND MOBILE PRODUCTS

SALES: \$3.60 billion

OPERATING PROFITS: \$324 million

ISSUES: Known primarily for niche, two-way radio products, the sector is growing respectably.

DATA COMPANY REPORTS

PCS networks are expected to be immensely popular. The first one in the S., Sprint Spectrum in Washington, C., signed up more than 80,000 subscribers in eight months (page 68). Like conventional cellular, PCS transmits calls over radio frequencies. But PCS is completely digital, so sound quality is better, more calls can fit on each frequency, and extra services such as wireless data communications are easy to add. And because PCS networks use many low-power transmitters instead of a few high-power ones, eventually the phones and the service charges should be cheaper. PCS has already taken root in Europe, where every country has agreed on a single technical standard called GSM. GSM is also spreading across Asia. In the U.S., though, there is no such consensus, which led to Motorola's first stake. It favors a format known as

cause we think it's the best technology in features and functions," says Jack Finlayson, corporate vice-president and general manager of Motorola's Pan-American Wireless Infrastructure Div. CDMA can, theoretically, carry 10 to 20 times as much traffic as standard analog cellular systems, while GSM offers a three- to sixfold capacity boost.

Problem is, many phone companies no longer buy that argument—or CDMA. Although about half of U.S. PCS networks are planned around CDMA, there are only a handful of commercial CDMA systems in operation, and just one in the U.S. Some phone companies that have tested CDMA say it delivers only six times the capacity of analog cellular—about the same as GSM. Since GSM has been used for years in Europe, it's a proven technology and components can be as much as 40% cheaper than com-

generates 31% of revenues and 38% of operating profits, is caught in a bind and in mid-July announced layoffs of 225 people. One of its biggest businesses, microcontrollers used in cars and appliances, is under assault from a rash of newcomers, including giant memory-chip makers seeking a more profitable niche. And the PowerPC, the Motorola microprocessor used in computers, is losing market

share. Beleaguered Apple Computer Inc., the biggest customer, reduced its orders by 25% in the first two quarters. "We need 20% market share of the computer business just to get to a stable position," laments Phil Pompa, director of marketing for Motorola's reduced instruction-set computing (RISC) microprocessor division. Right now, its share is only 7%.

Motorola's troubles show how quickly

a highflier can lose momentum. "You can fault the company for not reaching the tea leaves better," says Sood. "The core businesses are eroding faster than expected, and new products have yet become significant." That combination could signal the end of Motorola's reign as a corporate Golden Boy.

By Peter Elstrom in Chicago, bureau reports

A CELLULAR PIONEER WHO'S STILL DODGING ARROWS

Wayne N. Schelle was an early winner with cellular technology, and it looks like he has another hit. His startup, American Personal Communications, last November launched the nation's first personal communications services (PCS) network—ahead of AT&T and scores of others. "I would rather be like the Wright brothers and fly 150 feet than sit and wait for the Concorde to arrive," says Schelle (pronounced Shelly).

Schelle's company, of which a partnership of Sprint Corp. and cable-TV companies owns 49%, dubbed the service Sprint Spectrum; it already has more than 80,000 customers. The appeal: Customers don't have to sign a long-term contract and pay as little as \$15 per month, including use of a phone with a built-in pager and voice-mail capability. The response is more impressive when you consider that customers can't yet make or receive calls outside Schelle's territory, which stretches from Baltimore to northern Virginia.

Still, Schelle's battle has just begun. With other wireless carriers, he is pushing the Federal Communications Commission to force the Bells and other phone companies to stop charging wireless companies for connecting to their systems—on average, 3¢ per minute. The Bells, which don't pay wireless operators for calls going the other way, oppose the change. To Schelle and other PCS operators who paid millions for their licenses, winning the fight is crucial. Otherwise, "they can't be competitive," says Jonathan D. Foxman, a telecommunications consultant with



WAYNE N. SCHELLE

BORN Aug. 11, 1934, in Baltimore.

EDUCATION BA from Johns Hopkins University, MBA from George Washington University.

TELECOMMUNICATIONS CAREER Spent nine years at AT&T. In 1981, joined a paging and mobile-phone company; later started two cellular-phone operations. Began efforts in 1989 to launch a personal communications service, won a "pioneer" license in 1993, and launched the Sprint Spectrum service with partners in November, 1995.

PERSONAL Father of two. An avid gardener. Member of the Daffodil Society.

BIA Consulting Inc. in Chantilly, Va.

Adversity is nothing new to Schelle. A Baltimore native, he was the first in his family to graduate from college and earned his MBA at night from George Washington University. He spent nine years working for AT&T in various operations jobs and, in 1981, joined a local paging

and mobile-phone company, where he directed the launch of the Cellular One brand. After the owners sold out in 1984, Schelle started his own cellular company, which he sold to McCaw Cellular Communications Inc. in 1987.

OBSTACLES. In 1989, he caught wind of the first PCS systems, then being launched in Britain, and set out to create his own. At

SCHELLE'S GAME: His phone service will soon feel the heat of competition

American Personal, he holds the title of chairman and his son, Scott, is CEO.

The obstacles to bringing PCS to market, how-

ever, were many. For one thing, the portion of the spectrum that was most suited to carrying PCS calls was already in use. So Schelle's team came up with a technology that allowed PCS companies to share the spectrum with operators already using it.

As a reward for his early work on PCS, Schelle was granted a free "pioneer's preference" license by the FCC in 1993. But rivals griped about the freebie and he'll have to pay \$102 million for the license. Still, that's about 15% off what rivals paid in last year's auction.

Meanwhile, Schelle has his hands full. AT&T plans to roll out PCS in Washington next year.

Without a better deal on connection costs, Schelle's operation will have a hard time cutting prices enough to persuade consumers to adopt PCS as their basic residential service, his long-term goal. "Being first is great, but it does have its liabilities," Schelle says. For now, though, he soars alone.

By Amy Barrett in Rockville, Md.

STRIKING WHILE THE IRONS ARE HOT

Tommy Armour may have the next big thing in golf clubs

As any golfer knows, a case of the yips on the putting green can turn an otherwise solid golfer into a disaster. Maybe that's why Odyssey Sports, a putter business that Michael Magerman co-founded in 1990 and that Tommy Armour Golf acquired a year ago, is on fire, with sales expected to triple this year, to \$10 million. More than 160 professional Golf Association members use the unmistakable silver-headed club with a black insert that is said to put more feel into a putt—and possibly help the golfer's jitters.

Now, the 34-year-old Magerman, who became CEO of Tommy Armour as part of a buyout deal, is out to take up the irons business. He wants to loft Armour into the top tier of golf companies with the introduction in early August of a set of big-than-oversize clubs, the 100s, made from one of the hottest materials in the industry: titanium. "We've got the product that will make us No. 1 in irons," insists Magerman. "It's the replacement of every set of irons out there."

IT OF THE WOODS? Over the past two years, superstrong, lightweight titanium—which allows club heads to be made even bigger—has galvanized the irons market. Magerman is wagering that the promise of greater length and accuracy, and a larger sweet spot, can be transferred to irons—and any golfer willing to fork over as much as \$1,200 a set. With its irons intro-



HAIL, TITANIUM?

Magerman says Tommy Armour's new irons, 20% bigger than current oversize clubs, offer greater accuracy and a larger sweet spot

duction, Magerman is shooting for the same kind of breakout product that Callaway Golf Co. rode to industry leadership with its Big Bertha woods, or the more recent success Taylor Made Golf Co. has achieved with its Burner Bubble shafts. By most estimates, Armour, a

perennial also-ran, now ranks fifth among premium-priced club makers, behind Callaway, Taylor Made, Cobra, and Ping.

Thanks to stepped-up funding from its parent, conglomerate U.S. Industries Inc., Armour is slapping down marketing bucks: Its budget this year is up 40% over a year ago and will rise an additional 60%, to more than \$20 million in the fiscal year beginning Oct. 1. That will at least put it on the same course as its richer rivals. And the spending is shifting from print to high-profile TV.

The new irons will be introduced on national broadcast during the PGA Championship on Aug. 8-11 and will feature Dallas Cowboys Troy Aikman and Nate Newton.

The stakes are big for Armour and U.S. Industries. Armour is one of the smallest companies in USI's portfolio, and its earnings have been erratic. Last year, the company lost about \$1 million on sales of \$50 million, but with sales rising to an estimated \$87 million in 1996, Donaldson Lufkin & Jenrette Securities Corp. analyst Jack Blackstock reckons Armour will turn a profit of about \$6 million.

The irons launch is an outgrowth of the research and engineering center Magerman set up last year in Carlsbad, Calif., the Silicon Valley of the golf-club business. Its mission: work closely with designers and outside manufacturers to cut costs and reduce time to

market from two years to six months, critical in the ever-changing golf industry. One early obstacle: Magerman was told the irons would cost \$100 per stick to make, just about where he planned to price them. By reducing the weight in the grip and shaft, the engineers were able to wring enough cost out to make the irons viable.

A big hit with the titanium clubs will position Armour for an initial public offering, most observers and Magerman suggest. The danger, of course, is if the irons don't catch on—or are quickly copied by

TOMMY ARMOUR TAKES ITS SHOTS

MARCH, 1995 Acquires Odyssey Sports, a hot putter maker, and installs Michael Magerman as CEO of Armour

OCTOBER, 1995 Magerman combines R&D of Odyssey and Armour and opens new research center. Overhauls sales strategy to broaden appeal beyond low-handicap golfers

FEBRUARY, 1996 With backing of its parent, U.S. Industries, gains approval for a sharp increase in marketing and new-product spending

AUGUST, 1996 Prepares to unveil a range of titanium irons, which hold the key to the company's future growth

DATA BUSINESS WEEK

a larger rival, such as Callaway. Several industry sources believe Callaway's research and development team—like many industry majors—may be readying a titanium iron for the market. Bruce Parker, Callaway's head of merchandising and sales, will say only that his research team has been testing the material and studying products on the Japanese market. But, he adds, "we haven't seen anything with demonstrably superior performance." Another concern: Golf-equipment sales, after doubling from 1993 to 1995, to about \$1.5 billion, now appear to be flattening.

Skeptics argue that players change irons far less frequently than woods, and that they will be unwilling to spend several hundred dollars over the current premium price for clubs on an unproven product. Head pro Bob Ross of the Baltusrol Golf Club in Springfield, N.J., says he's "a little worried that titanium irons won't give you the same feel" as traditional stainless steel. Cobra Golf Inc. considered titanium for its new irons, due in September, but decided against it. Price was one issue, says CEO Mark C. McClure. Sheer size—in Armour's case, up to 20% larger than over-size—was another. "I believe there is an optimum size for irons, and in the rough, with more surface on the club head, it doesn't perform as well," McClure says, adding that he hasn't seen the final Armour version.

Despite the naysayers, Magerman is clearly making rivals take notice of Armour for the first time since the late 1980s, when the company introduced its wildly popular 845 series of irons. Its 1994 follow-up, the 855s, were late to market and by most accounts a disappointment. Armour's acquisition of Odyssey, and with it Magerman, brought some badly needed entrepreneurial flair to the company, which is named after a Scottish touring pro.

COPYCAT. Magerman was only a fair-weather golfer when he co-founded Odyssey in 1990. He had gotten out of the University of California at Los Angeles, gone to work for an interactive-TV outfit, and was studying for an MBA at night when family and friends staked him to starting a golf company. "I'm the first to admit I copied a lot of things from Ely Callaway," Magerman says. Five years later, he had a putter that was making a name for Odyssey and Tommy Armour knocked on his door.

Now, Magerman concedes, "we're betting the franchise." If Tommy Armour was looking for someone to take a hard swing at the competition when it tapped this young exec in a hurry, it certainly found the right guy.

By Richard A. Melcher in Chicago

Government

AVIATION

DANGEROUS LIAISONS?

U.S. airlines have ties with some questionable carriers



Few industries can match the airlines for global reach. Today, there are 340 nondomestic carriers flying in and out of America's cities. And major U.S. airlines are rapidly joining with foreign ones to serve an exploding market in international business travel. One problem: Few passengers realize that overseas airlines operating in the U.S. don't have to meet the strict safety standards that American carriers do. And the Federal Aviation Administration hasn't yet reviewed the civil aviation systems of almost half the 103 nations with carriers flying here.

A case in point: Taiwan's China Airlines Ltd. With 5.2 fatal accidents for every 1 million flights, 323 passengers have died on CAL flights since 1989 (based on 1982-1992 data, the latest available), according to the International Airline Passengers Assn. That puts it with Korean Air Lines, Thai Airways, Colombia's Avianca, and Air India as having among the worst safety records. All have accident rates at least 45 times as high as the world's safest carriers and six times the average rate of America's major carriers, according to IAPA. Yet all are allowed to operate in the U.S., even though they receive scant scrutiny from the FAA.

TIT FOR TAT. Officials at CAL stress they are working with U.S. officials to improve the airline's pilot training. "We are not satisfied with our safety record in our country," concedes Lee Wan-lee, a spokesman for Taiwan's Civil Aeronautics Administration. "I think our safety record will improve."

It's not that the FAA doesn't recog-

HONG KONG SLIP: Taiwan's China Airlines has a poor accident record

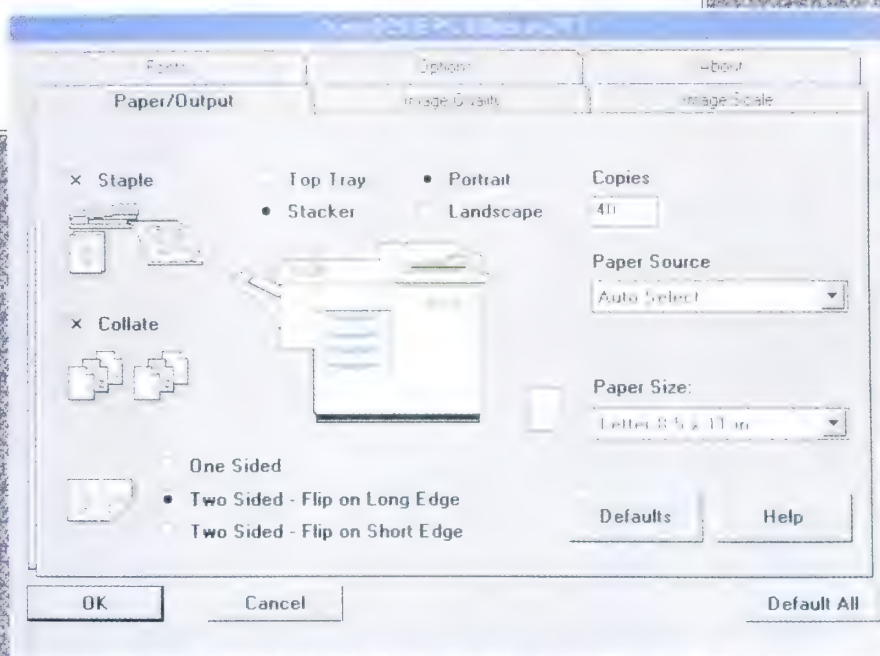
nize a growing global regulatory problem. In 1991, the agency launched an aggressive review of foreign civil aviation safety programs. The agency does assess foreign carriers directly, since it has little jurisdiction over them. Instead, in exchange for allowing another country's carriers to retain U.S. landing rights, countries must show American officials their systems either meet or are moving toward meeting minimum safety standards set by the Montreal-based International Civil Aviation Organization. But since ICAO does monitor airline safety, the FAA's program is the first time a consistent effort has been made to assess other nations' aviation safety. "Before this, an accident had to happen before the FAA took a look," says William D. Waldorf, president of System Safety Inc., an aviation-safety consulting firm in Prescott, Ariz. Crowds Barry L. Valentine, the FAA's assistant administrator for policy, planning, and international aviation: "This has been one of our success stories."

FAA inspections of foreign aviation authorities have led U.S. officials to bar airlines of Haiti and Surinam from U.S. airspace and to put restrictions on carriers from Guatemala, Turkey, and the Philippines. But the FAA effort has its costs, too. "These negotiations can be extremely sensitive diplomatically," says Valentine. Contentious and time-consuming, FAA confrontations with countries such as Colombia and Venezue-

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The FAA hasn't yet verified the safety standards of 46 of the 103 countries whose airlines operate in the U.S.

have strained relations with the U.S.

A more troubling result: Five years after its program began, the FAA still hasn't gotten around to verifying the safety standards of 46 of the 103 countries with airlines operating in the U.S., including those of Russia and China. Taiwan is due for an FAA review in October. Agency officials decline to disclose their schedule for reviewing other countries' authorities.

Valentine asserts that the FAA intends to complete all its assessments by the end of the year. "It's a top priority," he says. But critics scoff that an agency that took five years to review 57 nations cannot manage in five months to complete the remaining 46. After all, the FAA—its funding frozen by Capitol Hill and still in the midst of wrenching internal turmoil—is being forced to focus its already stretched resources on improving domestic air safety. Much of the pressure stems from the May 11 crash of ValuJet Flight 592 in the Everglades. "It's difficult to say what the FAA's priorities will be," says Marty G. Salfen, senior vice-president at IAPA.

DEALS GALORE. In the meantime, CAL and American Airlines Inc. are putting the final touches on a code-sharing agreement. The deal, typical of such arrangements, would make American and CAL appear as a single carrier to travel agents booking flights on computerized reservation systems. The agreement would also let CAL fly American passengers between Taipei and Los Angeles and San Francisco, with American connecting CAL passengers to some other U.S. cities. Continental Airlines Inc. announced a similar arrangement with CAL in January. Both "code shares" await U.S. approval. Consumer advocates complain that passengers can be confused by these alliances, unaware also that connecting flights abroad may be with a foreign airline. Even if they are aware, they may not know the safety record of the foreign carrier.

"Delta and American are turning over their good names and fortunes to some

of the most dangerous airlines in the world," charges David S. Stempler, president of Washington's AirTrav Advisors, a passenger watchdog group. Stempler spearheaded the IAPA review of foreign airline performance, which yielded the numbers the FAA relies on when consumers call the agency for such information. Stempler notes that American's access to booming Asian markets is severely limited under terms of the existing U.S. air treaty with Japan, a key gateway. So, Stempler asserts, "American is doing whatever it can to get access to Asia."

IAPA says has a fatality rate of 6.1 accidents per 1 million flights. American Airlines has teamed up with Poland's LOT to fly passengers from Chicago to New York to Warsaw starting in September; the FAA has restricted the Polish airline to just a few U.S. cities because of questions about Poland's oversight of its air system.

KEEPING MUM. While acknowledging that international travel is always a "major concern," FAA officials stress that air travel remains the safest form of transportation in the world, even under less stringent international

standards. Says Jeffrey N. Shuman, a lawyer representing airlines who is also a former assistant secretary for international aviation at the Transportation Dept.: "The statistical probabilities of anyone coming to grief" are far less on a plane than on any other mode of transport.

Still, the FAA won't disclose to consumers any details about the failings of overseas carriers, complains Michael Schaeffer, CEO of Woodside Travel Trust, a large global business-travel management company. "The FAA requires that airlines' on-time performance is available to passengers," Schaeffer says. "Why not safety information on foreign carriers?"

Airline executives defend the new alliances, saying they will help weaker airlines achieve higher standards of safety, while providing them with greater access to foreign

lands. "You don't sign a code-sharing agreement with an airline you don't believe is safe," insists United CEO George Greenwald.

But neither the FAA nor the State Dept. offers even rudimentary safety data on specific foreign carriers for traveling public, Schaeffer complains. That means many of the 19.4 million U.S. passengers flying overseas each year must base their decisions on little more than a hunch. And that could make for a rough ride.

By Christina Del Valle, with Scott Crock in Washington and Jonathan Moore in Taipei

Flying With Whom?

Less-regulated foreign operators are forging marketing links with some of America's major airlines

AIRLINE	FATAL ACCIDENTS*	COMMENTS
CHINA AIRLINES (TAIWAN)	5.2	Awaiting U.S. approval of code-sharing deals with Continental and American. Had a major accident in each of the past six years. The FAA has still not reviewed Taiwan's aviation regulatory authority.
KOREAN AIR	5.2	Has a code-sharing arrangement with Delta. The FAA has not yet completed its review of Korean aviation regulations.
POLISH LOT	NA	A code-share partner with American. The U.S. has frozen air service from Poland to problems with the Polish regulatory authority.
THAI AIRWAYS	6.1	Recently received approval to link with United. The FAA has yet to complete its review of Thailand's aviation authority.

*Per 1 million flights, U.S. Airline average = 0.76

NA= Not Available

DATA: INTERNATIONAL AIRLINE PASSENGERS ASSN., FAA, BUSINESS WEEK

American Airlines declined comment. But Continental says the Taiwan carrier has greatly improved its maintenance and pilot training and that CAL will use nearly new planes on the pending code-shared routes. "It's a totally different company than when those accidents occurred," says a Continental spokesman.

No question, the deals are proliferating. Delta Air Lines Inc., for example, has signed a joint venture with Korean Air, which also has had 5.2 fatal accidents per 1 million flights. United Airlines Inc. recently received approval from the Transportation Dept. to join forces with Thai Airways, which the



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HOW FORD'S F-150 LAPPED THE COMPETITION

With some demographics, a little history—and a midlevel designer in the basement

The atmosphere was boisterous and festive as about 400 Ford Motor Co. designers and engineers gathered late last month to celebrate the success of the hot-selling F-150 pickup truck. Ford executives sipped cocktails, nibbled hors d'oeuvres, slapped backs, and applauded members of the F-150 team in speeches from the podium.

But when James E. Englehart, Ford's vice-president for light-truck development, singled out the efforts of one mid-level design staffer, he took the room by surprise. So obscure was the designer, James C. Bulin, that higher-ups had forgotten to invite him. Fortunately, Bulin heard the noise from down the hall and came by in time to hear Englehart praise him for "having a real impact on the direction we took with this truck."

MAVERICK. Englehart wasn't just blowing smoke—and Ford execs aren't likely to overlook Bulin again soon. The sinewy, sculptured F-150 is Ford's hottest new model since the Mustang tore up the streets in the mid-'60s. Sales of Ford's F-series pickup trucks are up 18% since the F-150's redesign was launched in January. Altogether, the F-series could sell 800,000 trucks this year, easily retaining the lead as America's top-selling vehicle. "This launch has exceeded our wildest expectations," gushes Ford Div. General Manager Ross H. Roberts.

For that, Ford executives can largely thank Bulin, 55, a maverick who has

spent most of his career operating on Ford's fringes. Working out of the basement of Ford's design center, Bulin and his bookish sidekick, auto consultant John Wolkonowicz, created an automotive anthropology by pinpointing the tastes and characteristic values of six generations of 20th-century Americans (table). By using Bulin's generational "value groups," Ford was able to tailor the design and marketing of the truck so that it would "hit the hot buttons" of baby boomers, says Bulin. "We developed a way of crawling inside the heads and hearts of tomorrow's customers."

Bulin's research helped Ford design a trimmed-down model packed with family-friendly features—and boomers are taking the bait. Although the over-50 crowd rang up two-thirds of the old model's sales, boomers are expected to buy 80% of the new F-150s. Peter Palestri, 40, recently chose a black F-150 Supercab over a Lexus luxury sedan when he searched for a new car. "It rides as nice as the Lexus

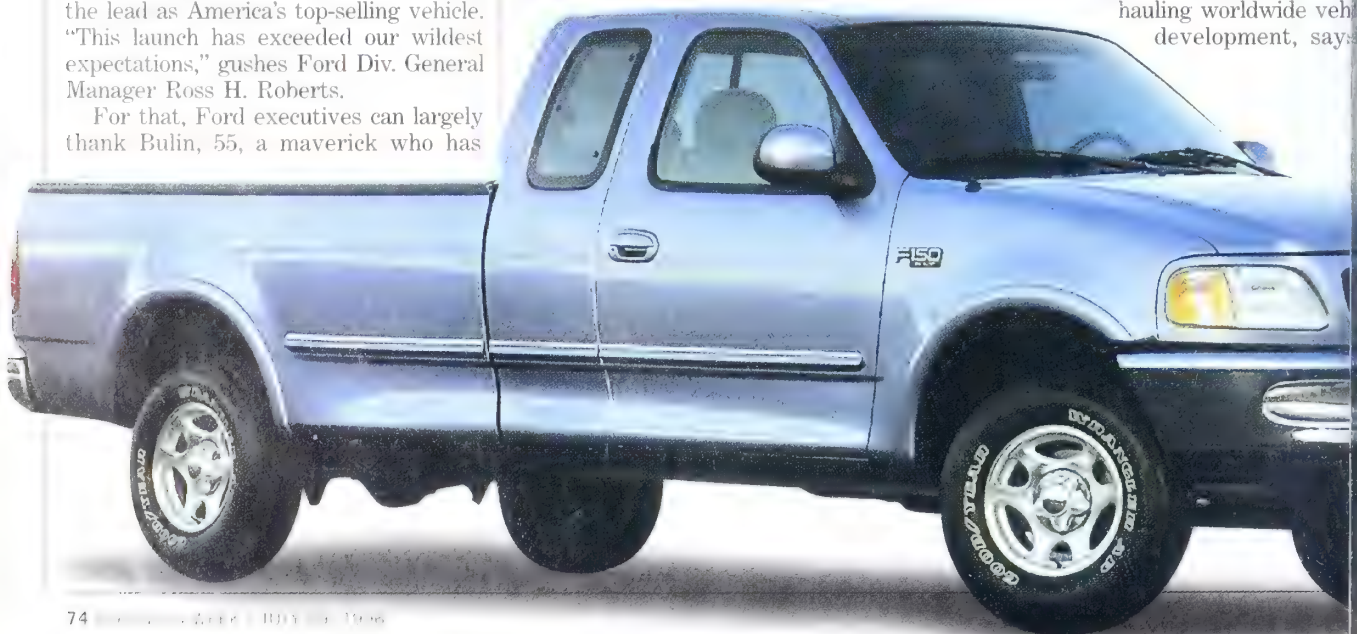
and my three kids fit very comfortably in the backseat," says Palestri, who owns a landscaping company in Morristown, NJ. "We use it as our family vehicle."

And Wall Street is applauding the beefier \$4,000 in pretax profit each vehicle should generate on average, double what the old model mustered. While the F-150 starts at \$15,455, buyers are snapping up heavily equipped models such as the four-wheel-drive Supercab, which goes for \$25,800. Thanks in large part to the F-series—which accounts for 25% of Ford's vehicle sales—Ford's second-quarter earnings jumped 21%, to \$1.1 billion. For the year, J.P. Morgan & Co.

analyst David Bradley estimates profits will rise 18%, to \$4.6 billion, on revenues of \$118 billion.

That may be just at the beginning. Although Ford senior execs first thought Bulin's approach kooky, analysts say it could completely change how Ford develops and markets its cars. Jacques A. Nasar, the influential group vice president in charge of overhauling worldwide vehicle development, says at

The heavily equipped Supercab, at \$25,800, is a favorite among buyers



become "one of the building blocks" of product development. "Jim Bulin is a wizard at this stuff," says Nasser. "It is us a competitive advantage."

Indeed, with its focus on using customers' desires as a starting point for design—rather than simply benchmarking rivals' cars—Bulin's approach marks a step forward for Detroit. In the past, carmakers have not used extensive consumer research at the very beginning of the redesign process; instead they tended to start by tearing apart rivals' successful cars.

DATE. The roaring success of the F-150 compared with the sputtering start of Taurus illustrated the limits of Detroit's traditional route. Taurus developers shifted their sights on beating the highly entered Toyota Camry. But the changes needed Taurus prices near \$20,000, scarce for consumers. The Taurus now needs a \$3,000 rebate to keep the Honda Accord competitive. Bulin's approach allows designers to better predict what buyers really want, says Nasser, who adds that Ford no longer develops cars by copying rivals. "You're always looking backwards," he says.

Of course, psychological market research on boomers and other generations has been around for years. But Made-Hochstein, president of DYG Inc., a New York social and market research firm headed by the renowned consumer researcher Daniel Yankelovich, says that

NASSER: As product-development VP, he will use Bulin's offbeat approach

Bulin's approach has made such demographic tools far more useful. Its predictive powers offer a clearer method of designing products to anticipate the needs of targeted consumers. "In 10 years, this will be used much more broadly, and well beyond the auto industry," says Hochstein.

Yet for all its success, Bulin's work developed almost by chance. As Ford began planning to overhaul the truck in late 1989, he was given the mundane assignment of putting together a pictorial history of truck design. Bulin brought in Wolkonowicz, an automotive history buff who had worked at Ford before joining consultant Arthur D. Little Inc. in 1986.

Bulin and Wolkonowicz quickly figured out that pickup-truck design had not really changed for a generation. Frustrated, they commiserated over beers one night at Miller's Bar in Dearborn and hatched a plan to expand the project on their own.



They soon added different images to the truck pictures they had affixed to giant, rolling bulletin boards. As photos of cars, trains, planes, radios, and toasters were added, they had a history of consumer products of the 20th century. They noticed that designs changed at similar times, but they didn't know why. "We started looking for what was driving people to make different choices," recalls

Wolkonowicz, 45. Next came information about pop music, movies, fashion, wars, and economic hardship.

From that kaleidoscope of images, Bulin hatched what Ford came to call its value groups strategy. Bulin concluded that the basic values that motivate purchases are instilled in each generation between their teens to mid-20s, formed by everything from their relationships with their parents to whether their lives were touched by war and the movie stars they worshiped. "The growing-up experience of each generation establishes the rules they live by," Bulin says.

The real challenge was translating

Generation Gap

Developers of Ford's hot new F-150 pickup identified six distinct generations, each with shared traits and tastes that influence its car-buying habits. Ford is using these generational "value groups" to help develop a new luxury car, a sport-utility vehicle, and the next-generation Thunderbird.

	PERSONAL VALUES	CAR VALUES
DEPRESSION IS 1920-34	Because of attitudes formed during the Great Depression and World War II, they always plan for a rainy day. They are also status seekers.	They like new models and trade up every year. They like cars that are longer, lower, wider, and more colorful. They believe trucks belong on a farm or construction site.
GIET GENERATION 1935-45	Childhood of postwar peace and prosperity made for an extended period of innocence. Little parental pressure and lots of free time. Their movies idealize humble heroes.	They fondly remember their hot rods. Prefer cars with individuality to generic lookalike vehicles. They have not embraced trucks, except for custom wheels.
BOY OMERS 1946-64	The first TV generation. They were indulged by their parents and pushed to win. They seek instant gratification and want others to think they make smart purchase decisions.	They view cars as appliances. They have embraced minivans and sport-utility vehicles for their commanding road presence and lots of creature comforts. As they begin to buy pickup trucks, they're looking for the same.
POST GENERATION 1965-69	Disenfranchised because they grew up in the boomers' shadow. Hurt more by parental divorce, they're waiting for life to get better and are not affluent.	They drive small sport-utility vehicles and offbeat niche vehicles. They buy used cars because many cannot afford to buy new cars.
BIRTH DEARTH 1970-77	Grew up in the rich 1980s and acquired a taste for excellence, but their jobs won't support that. They've become practical, focused, and future oriented.	They drive sport-utility vehicles and practical sedans. A Jeep Wrangler is a sports car to them.
BABY BOOMLET 1978-present	The children of the boomers. They have a strong desire for the affluence of their parents' generation, though they're unlikely to have as much money.	Still forming. But their generation will be nearly as big as that of their parents, so they will have a huge impact on future products and marketing.

The Corporation

those insights into design changes. With the F-150, Ford designers first wanted to style the truck like a big rig. But that idea died after Bulin showed that boomers value compact designs found on Japanese cars they came of age with.

But that didn't mean boomers still didn't expect a pickup truck to look powerful; instead, they defined power differently from earlier generations. One reason: Starting with President John F. Kennedy's National Council on Physical Fitness, which pushed exercise in public schools, boomers have grown up with a passion for staying in shape. That, Bulin argues, has led them to equate strength with being trim and fit, and they seek out sleek products. Bulin's data convinced Ford's designers that the F-150 would have to look lean and muscular to succeed. So Ford narrowed the cab by two inches and lengthened it by five. "Once you establish those key strategies, it was hard for a designer to jump off the cliff," says Thomas D. Baughman, the F-150's chief engineer.

Bulin's unconventional approach grew quietly at first, but eventually it influenced everything from the wheel size to the F-150's doors. Bulin's analysis showed that while boomers expected a pickup to have a commanding "presence," they also wanted comfort. So Ford increased the wheel size to make the truck taller but smoothed out the tire tread so it would ride like a car. The nose is compact and almost carlike, which added passenger space. On the six-seater F-150 Supercab, Ford added a rearward-swinging third door tucked behind the front passenger door that makes hopping in the back easier—a big draw for boomers with growing children. "The value group research was the reason we read the need for the third door," says Edward E. Hagenlocker, president of Ford's auto operations.

EASY ACCESS. Now Ford is spreading Bulin's tactics to other models. Company sources say an entry-level luxury car and a sport-utility vehicle for the youth market are receiving the generational treatment, as will the Thunderbird.

Bulin's approach also helped shape the design of the Expedition, the full-size sport-utility vehicle Ford is introducing on Oct. 2. The Expedition shares nearly half the F-150's parts, including its softly

sculptured front end. And as with the pickup, Bulin helped Ford shape it to the needs of baby boomers. To add more passenger space, Ford shortened the front doors on the four-door model, offering easier access to the back rows of seats.

With such well-targeted goodies, Wall Street expects a huge hit. Ford is predicting annual sales of 150,000 to 200,000. Analysts say the Expedition—expected to be priced between \$35,000 and \$40,000—could add up to \$1 billion to earnings. "This will be a category-killer," says J.P. Morgan's Bradley.

It's all a far cry from the early summer days of 1990, when Bulin and

But Bulin's data drove home the idea that if Ford kept to the tried-and-true baby boomers wouldn't buy it. "We realized we could offer a vehicle to a generation that might be dying off," recalls de Jonckheere. "This gave us courage not only to get off the diving board but once we got in the water, to keep swimming." Bulin also won a key ally: In 1990, after Hagenlocker, then vice-president for truck operations, saw the approach he boosted funding and backed it.

Sticking with the approach took some courage. Traditional truck buyers dislike some of Ford's softer designs in car consumer clinics in 1991 and 1992. Although boomers liked a rounded look

BOOMER ROOM: The '97 Expedition sport utility puts a premium on space



reminded them of minivans, ranchers and hardhats who have none of it. Under Ford's old development system, the criticism from traditionalists might have frightened the team into retaining an old boxy design. But the backup for

Wolkonowicz began rolling their giant bulletin boards around to show off their nascent research. By then, they had divided up the generations into six groups, beginning with Depression Kids, born from 1920 to 1934, and ending with the Baby Boomlet, children born since 1978. From those groups, they eventually distilled their data into 30 customer segments—another radical change for Detroit, which traditionally sliced the market by products, not people.

But the two were still working out of a cramped basement office evenings and weekends, while handling their regular design assignments during the day. Finally, they showed the giant boards to project manager Baughman and his boss, Terry de Jonckheere, then program director for full-size trucks.

The two were fascinated by what they saw. They had faced pressure to stick with the traditional lines that had made the F-150 a sales leader. High-level execs warned them not to butcher the company cash cow with a radical redesign. "Nothing that the company was doing represented more profit opportunity or sales volume," recalls Andy Sarkisian, who became the first marketing manager for the new F-150.

Bulin's data helped the modern design win, says Hagenlocker. "This allowed us to stretch, and as we went along, stretching became more comfortable," he says. **JITTERS.** Yet before the F-150 proved to be a home run, some top Ford executives wondered if the value groups strategy might push the all-important truck too far. And as the auto maker came under criticism for the unusual ovoid styling of the 1996 Taurus, executives grew even more jittery. "A lot of people reckoned we went too far," recalls Andy Jacobson, the F-150's design director.

But as F-150 sales have soared, so has Bulin's stock. Even though he didn't get asked to the June celebration, he's now getting plenty of invitations to share secrets with Ford's product developers. And Bulin was recently asked to be Chairman Alexander J. Trotman and Hagenlocker for lunch on Aug. 7 to celebrate the F-150's success with the rest of the team. "Everybody's interested," Bulin says, chuckling. "They are warmed up, the thing having actually proven itself. That may have surprised many at Ford but not the guys who built it from the ground floor up."

By Keith Naughton
Dearborn, Mich.

HAPPY MEALS FOR McDONALD'S RIVAL

In the Philippines, Jollibee is trouncing the giant

The golden arches of McDonald's Corp. are among the world's best-known corporate symbols, assuring that their Big Mac will look and taste the same whether ordered in Manhattan or Malaysia. That consistency helped McDonald's build the most successful fast-food brand in the world. But it has also created an opportunity for the competition, at least in one market. A family-owned chain in the Philippines, Jollibee Foods Corp., has borrowed every marketing trick in the McDonald's book, from child-friendly characters to prime locations. But instead of selling a generic burger available in any market in the world, Jollibee caters to a local penchant for sweet-and-spicy flavors, which it incorporates into its fried chicken and spaghetti, as well as burgers. "We've designed these products to suit the Filipino palate," says Menlou B. Bibonia, Jollibee's marketing vice-president.

AND SPICE. The combination of fast service and tailored menus helped Jollibee become the dominant chain in the Philippines—though restricting foreign ownership of restaurants has helped, too. Sales figures are unavailable, but a market survey by A.C. Nielsen Co. affiliate Pulse Research Group shows that Jollibee has 46% of the Philippine market, vs. McDonald's 16%, based on share of total hamburger-restaurant visits. Jollibee has 177 outlets in the Philippines—roughly double McDonald's total of 85—and is opening an additional 36 this year. In the U.S., Jollibee is trying to expand to other markets, mostly in the Southeast. It also plans to open stores in Los Angeles and San Francisco, which have large Filipino communities, later this year. Jollibee's strength is its understanding of

local tastes. Besides the spicy sauces, it offers rice with its entrées. "The Jollibee burger is similar to what a Filipino mother would cook at home," says Tessa M. Puno, an analyst at Philippines-based Abacus Securities. And the fact that Jollibee's prices are 5% to 10% lower than McDonald's doesn't hurt, either.

Jollibee's success has not gone unnoticed. McDonald's has introduced its own Filipino-style spicy burgers—one of the few instances in which the chain has changed the actual burger patty. McDonald's officials in Manila would not comment on their franchise operations, and at the company's Oak Brook (Ill.) headquarters, a spokeswoman had little to say about the Philippines: "We focus on our customers there just as anywhere else."

Just like the U.S. chains, Jollibee works hard to woo kids with in-store play activities and a line of heavily advertised signature characters including a spaghetti-haired girl named Hetty and a hamburger-headed boxer called Champ, among others. Licensed toys, towels, and other novelties promoting the bunch are for sale in stores.

Jollibee didn't always have the edge. The chain battled McDonald's through the 1980s, and the two were neck-and-neck until 1989 when a military coup caused foreign businesses such as McDonald's to pull back from the Philippines. Jollibee added 30 outlets in 1990. With \$250 million in sales in 1995, the

JOLLIBEE'S RECIPE FOR BEATING McDONALD'S

- Cater to local tastes with heavy, sweet-spicy sauces
- Surround McDonald's outlets, pick prime spots
- Target kids with ads and play activities
- Keep to high standards of fast service, cleanliness
- Price food items 5% to 10% lower



SWEET SPOT: Jollibee has 46% of the local market

chain is the second largest consumer goods company in the Philippines—but minuscule compared with McDonald's at \$29.9 billion in worldwide sales.

EASTWARD, HO! Now, Jollibee is trying to find other niche markets where it can dominate. It has 15 restaurants in Southeast Asia and the Middle East and plans to add 14 to 18 more this year, along with the stores in California. Longer term, it thinks Chicago, New York, Houston, and Miami, with their Asian and Hispanic populations, could be good prospects.

Meanwhile, the competition in Jollibee's home market could intensify. Restrictions that prohibit foreign companies from owning stakes in retail chains are expected to be lifted within the next two years, allowing McDonald's to operate its own stores. "They could pour money in here to buy advertising, to secure prime locations—to put pride before profit," says Tony D. Kitchner, vice-president of Jollibee's international unit. Or maybe to remind other burger-chain wannabes around the world of the might of the Golden Arches.

By Hugh Filman in Manila



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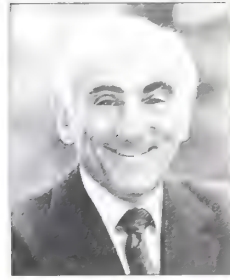
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EDITED BY AMY DUNKIN

LUSH LANDSCAPES THAT DON'T WASTE WATER

When horticulturist Thomas Christopher transformed his yard from green lawn and trim boxwoods to a colorful and tumbling flower meadow, his neighbors in Middletown, Conn., wondered if he had lost his marbles. "My yard is a bit out of the ordinary," he admits. Indeed, during the summer, orange tiger lilies visually set his suburban eighth of an acre on fire. "It stops traffic," he says.

It also saves water. Christopher's blazingly beautiful pasture thrives on rainfall alone while his neighbors sprinkle and soak their turf grass only to have it burnt brown by August. Approximately 50% of the nation's drinking water goes to irrigate landscapes, according to the Environmental Protection Agency. And with drought conditions and population growth straining many states' reservoirs and aquifers, more

homeowners are looking for alternatives to the minifairways that have become the residential standard. "With water shortages causing water bills to soar, people have been forced to realize that water is a precious resource," says Doug Welsh, extension horticulturist for Texas A&M University in College Station.

This realization, together with the hassle of tending a traditional lawn and hedge landscape, has fueled a nationwide shift toward low-maintenance, water-wise gardening, or xeriscaping (*xeros* is Greek for dry). Officials with county agricultural offices and city water departments coast to coast (particularly in Arizona, California, Colorado, Florida, Georgia, New Jersey, New York, Texas, and Wyoming) say they can't assemble enough folding chairs for homeowners interested in learning about water-thrifty horticultural tech-

niques. "The movement is truly taking hold," says Ken Ball, landscape architect and conservation specialist with Denver Water. President Clinton even recently signed an executive order mandating that all federal buildings be xeriscaped—an action that follows passage of similar water-wise planting laws that apply to state buildings in California and Texas.

TURF, TOO. Does this mean cactus and rock formations for all? Absolutely not, says Richard Weir, horticulture educator at Cornell Cooperative Extension in Plainview, N. Y. "Xeriscaping doesn't mean you have to construct a desert." Nor does it necessarily entail tearing up turf

croclimates (areas of shade, windbreaks, etc.), existing vegetation, and topographical conditions of the site is the first step. "Take a survey of your yard, especially during the dry summer months. What's thriving and what's not doing well?" says John Kavouras, water conservation planner with the Southwest Florida Water Management District. Plants that are killed despite supplemental watering send a clear message that they're ill-suited to the environment. Next, analyze the soil to determine various types of plants the ground can sustain and if soil amendments—such as organic compost to boost moisture retention—are needed to support other desired types of vegetation. Most nurseries sell do-it-yourself soil analysis kits.

Seven Steps to a Water-Wise Garden

- 1** Take a survey of your yard to determine topographical conditions, microclimates (areas of shade, windbreaks, etc.), and health of the existing vegetation, especially during the dry season
- 2** Analyze the soil and use such additives as organic compost to boost water retention
- 3** Limit turf areas and use water-thrifty varieties of plants
- 4** Group plants with similar water needs together and emphasize drought-tolerant species
- 5** Mulch to limit evaporation, stifle weeds, and prevent erosion
- 6** Irrigate efficiently, avoiding fine-mist sprinklers and relying on slow-drip systems, such as bubblers and soaker hoses
- 7** Maintain the landscape by fertilizing, pruning, and applying pesticides—but don't overdo it

DAVID R. WELSH



in favor of tiger lilies. "You can have a lush lawn and formal plantings. It's a matter of how you go about it," he says.

Developing an awareness of the regional climate, mi-

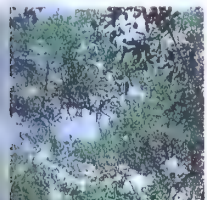
Once familiar with the lay of the land, it's time to come up with a design. Arrange plants according to thirst is key. "The idea is to group plants with similar water requirements together," says Dick Pearson, a supervisor with the Planning, Environmental Conservation Services Dept. in Austin, Tex. This prevents overwatering one species

attempt to quench another. "Don't put impatiens next to cactus," he says. Also don't put the cactus in a shady place where the rain gutter empties, or the impatiens on a very slight slope that loses water to gravity.

In general, you want to plant that requires intense

watering. Terry Lewis, a landscape architect in San Antonio whose designs have repeatedly won the city's annual xeriscape competition, recommends reducing thirsty sections by installing or ending bedding areas filled

with drought-tolerant vegetation. "Not only does it save water, but it creates a stronger, more interesting landscape," he says.



GARDENING

Plants with shiny or small leaves, fleshy roots, spiny stems, and hairy foliage are good bets because they are structurally suited to retain water (fleshy roots hold more liquid and hairy leaves trap moisture). To help

them along, mulch. Wood bark chips, pine straw, nut-

shells, and landscape clippings, layered two to four inches thick, cool the ground and reduce water evaporation as well as deter weed growth and prevent erosion.

For those unwilling to part with their grassy expanses,

perhaps a water-thrifty turf will do. Slow growing varieties such as buffalo grass, blue grama, and turf-type tall fescue look much like traditional lawn cover. "You just don't have to mow or water them as often," says Cornell's Weir. But come watering time, do so efficiently. Water your lawn, shrubs, and trees separately according to need rather than a fixed schedule. Early morning or evening applications are best during spring and summer. Otherwise, the midday heat causes 30% of the water to escape into the atmosphere before it ever hits the ground.

Regardless of the time of day, avoid fine-mist sprinklers that emit sprays more conducive to evaporation than irrigation. Slow-drip systems (bubblers from which water bubbles upward or soaker hoses that release water through small holes) are effective alternatives, especially for trees and bed plantings that benefit from an even stream of water delivered to the soil directly above

Xeriscaping Resources

Waterwise Gardening

By Lauren Springer
Prentice Hall Gardening, \$9

Water-wise Gardening: America's Backyard Revolution

By Thomas Christopher
Simon & Schuster, \$25

Xeriscape Gardening

By Connie Ellefson, Tom Stephens, and Doug Welsh
MacMillan, \$30

DATA BUSINESS WEEK

much he is watering, he puts coffee cans in his garden to measure the accumulation.

Finally, keep up with the yard work. Plants that are pruned, pest-free, fertilized, and adequately mulched are less stressed, which reduces their need for water. But be careful not to overdo it. Denver landscape architect Jim Knopf says xeriscapes don't need as much attention as other types of gardens because they are adapted to the environment. In fact, he warns, excess fertilizer and pesticide weaken otherwise hearty plants and increase their thirst.

Converting lawns and gardens into xeriscapes need not be a chore. "There's no

law that says you have to do everything all at once," says Kavouras at Southwest Florida Water, suggesting that simply mulching plant beds will create a more water-wise garden. Or accent that sternly clipped hedge with drought-resistant shrubs—like chocolate flower, which smells like chocolate milk, or red fountain grass, which is crowned by pink tufts of fluff. "Xeriscaping allows you to deviate from the cookie-cutter landscapes we've grown accustomed to and be creative," says Denver Water's Ball. That has a certain grassroots appeal.

Kate Murphy

THE SECRETS OF THIS GARDEN

One of Terry Lewis' award-winning xeriscape designs in San Antonio. Among the drought-resistant plants he used: Mediterranean fan palms by the pool, yellow-flowered lantana, foxtail ferns, Asiatic jasmine for ground cover and purple-flowered salvia greggii

their roots. It's a widespread misconception that plants need water on their foliage. It's the roots that do all the drinking.

YARD WORK. Peterson at Austin's Conservation Services Dept. says the most common gardening error is overwatering. He recommends irrigating deeply (one inch of water) once every four or five days to encourage strong roots that reach far into the soil for moisture and nutrients. If the ground is too dry and water starts to run off, "quit watering and come back later to finish up," he says. To keep track of how

GAINING AN EDGE WITH HEDGE FUNDS

Wanted: protection from a downturn in an aging bull market. For many well-

heeled investors, hedge funds seem to be the answer. This year, hedge-fund assets have swelled above \$100 billion—

SMART MONEY

more than regaining the ground the industry lost in 1994, when assets dropped 20%, to \$74 billion. "If and when the market turns negative, investors expect hedge funds will make money or not go down as much as the market as a whole," says E. Lee Hennessee, a director of WPG-Hennessee Hedge Advisory Group in New York.

That has been the case in the past. Take 1987, the year of the crash. While the Standard & Poor's 500-stock index posted a 5.24% gain, and growth mutual funds squeaked out only 1.02%, hedge funds returned 14.49%. Again, in 1990, when the S&P and equity growth mutual funds registered negative returns of 3.11% and 3.82%, respectively, hedge funds finished the year up 10.97%. Hedge funds don't have to stay fully invested in the market like most equity mutual funds, and they have the flexibility to hedge with put options and short speculative securities.

LONG AND SHORT. But while hedge funds do well during sluggish times, they underperform during strong bull markets because of their hedged bets, or shorts, on declining stock prices. Indeed, in 1995, the S&P returns soared past those of hedge funds, 37% vs. 15%. Still, from 1990 to 1995, hedge funds had a compounded annual

return of 21.9%, vs. 16.6% for the S&P, according to WPG-Hennessee.

By definition, hedge funds are private investment limited partnerships that restrict the number of investors to 99 or fewer to avoid Securities & Exchange Commission regulations. Initially, the funds simply bet long and short on equities to reduce market risk. But now there are a dozen hedge-fund strategies, some of which may not even use hedging. For instance, George Soros' Quantum fund and Julian Robertson's Tiger fund—called macro funds because they try to profit from macro-economic shifts worldwide—make bets on global currency, bond, equity, and commodity markets but don't necessarily hedge their positions. Event-driven strategies—such as risk arbitrage, which focuses on mergers, and distressed securities, which involves purchasing debt and equity of reorganized or bankrupt companies—also may not hedge.

Other approaches that use hedging regularly include the market-neutral funds, which go equally long and short, and levered bond funds. Derivatives, options, and futures are often used. "Hedge funds are as different from each other as the managers are," says Peter DeCicco, a hedge-fund consultant in Fairfield, Iowa. Some are more exotic, such as the macro funds, while others, like Phoenix LP,

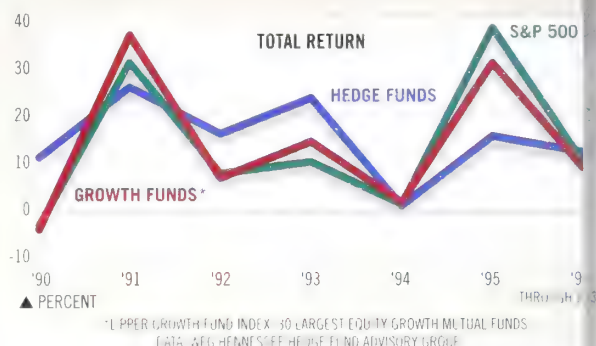
use a classic long/short strategy. "You're taking on manager risk in a hedge fund rather than the market risk in a mutual fund," says DeCicco. Investors are buying the manager's philosophy, not the stock market.

The majority of these funds only accept accredited investors, whose net worth exceeds \$1 million or whose annual income tops \$200,000 for an individual or \$300,000 for a couple. Fund liquidity is limited, and investors get scant disclosure about investments. Also, managers often have a large portion of their own net worth invested with the fund. In return for the expected above-average returns, managers earn a gen-

eration management fee on top of the fees of the underlying funds. Alpha Latin America posted a 102.7% return for the three years ending January 30, while Ultima Investment turned in 58.6% and Haystack Multiple Strategies 53%, according to the *MAR/EDGE* newsletter. But these are stellar performers. Generally all returns for the fund group have trailed those of regular hedge funds and the S&P, according to Hedge Fund Research, a Chicago-based consultancy. Industry consultants say investors should improve their more careful choice of funds that complement one another's strategies.

Still interested in investing

HOW HEDGE FUNDS MEASURE UP



erous 20% of the profits plus a 1% management fee.

For investors who can't afford the required \$500,000 or \$1 million minimums, a fund of funds may be an option. It's a hedge fund that invests in a portfolio of hedge funds, allowing investors to come in for \$100,000 or less. Investors get access to managers who would otherwise be off-limits, but they must still pay a 20% performance fee and 1%

ing in a hedge fund or fund of funds? Unfortunately, it's somewhat of a clandestine world. Because the SEC prohibits hedge funds from advertising, "there is no stop shopping like there is for mutual funds," says Antoine Bernheim, publisher of *U.S. Offshore Funds Directory* (212 371-5935). He leaves the investor with two options: hire a consultant to find a fund, or network through friends.

Before you entrust your money to any manager, make sure you know his or her track record. Consider the fund's strategy, how it controls risk, and how much leverage is used. Hedge funds require both resources and resourcefulness to be considered a viable investment option.

Toddi Gura

Popular with wealthy investors who feel the bull has run its course, hedge funds range from straightforward to the exotic

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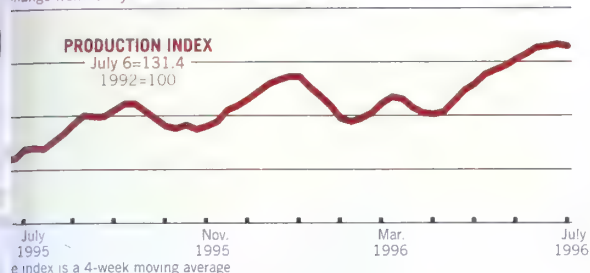


Published by Marketing Direct Concepts

Business Week Index

PRODUCTION INDEX

Change from last week: 0.2%
Change from last year: 7.7%



production index edged down during the week ended July 6. Before publication of the four-week moving average, the index fell to 130.9, from 131.4. Auto and truck plants were closed for most of the week in observance of Independence Day, and many lumber mills shut down for yearly maintenance. Seasonally adjusted output of steel and rail-freight traffic increased for the week.

Leading index will be unavailable for an indefinite period of time.

Source: Index compiled by The McGraw-Hill Companies

ADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
CK PRICES (7/12) S&P 500	646.19	657.44	15.6
PORATE BOND YIELD, Aaa (7/12)	7.89%	7.79%	6.8
USTRIAL MATERIALS PRICES (7/12)	106.2	105.6	-8.1
INESS FAILURES (7/5)	NA	NA	NA
L ESTATE LOANS (7/3) billions	\$521.8	\$508.2	6.6
IEY SUPPLY, M2 (7/1) billions	NA	NA	NA
IAL CLAIMS, UNEMPLOYMENT (6/29) thous	351	354r	-4.6

Sources: Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept.

TEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
ERIAL FUNDS (7/16)	5.20%	5.14%	5.72%
IMERCIAL PAPER (7/17) 3-month	5.55	5.54	5.77
TIFICATES OF DEPOSIT (7/17) 3-month	5.54	5.55	5.75
ED MORTGAGE (7/12) 30-year	8.55	8.36	7.64
USTABLE MORTGAGE (7/12) one-year	6.15	6.07	5.78
ME (7/16)	8.25	8.25	8.75

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

r data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

ERIAL BUDGET

Friday, July 22, 2 p.m. EDT ► The Treasury will likely report a budget surplus of \$116.8 billion for June when quarterly corporate and individual tax payments are due. According to the median forecast of economists surveyed by MMS International, of The McGraw-Hill Companies, the projected surplus is more than double the \$48 billion posted in June, 1995. But a surprise in the calendar last year meant that social security payments were made in June. On July 16, the Office of Management & Budget said that the deficit for fiscal 1996 is \$116.8 billion for fiscal 1996, which ends in September, and the Congressional Budget Office put it in the range of

\$115-\$130 billion. The 1995 deficit stood at \$164 billion.

DURABLE GOODS ORDERS

Thursday, July 25, 8:30 a.m. EDT ► New orders taken by durable-goods manufacturers likely declined by a small 0.5% in June, forecasts the MMS report. However, the National Association of Purchasing Management has already reported a big gain in its new-orders index for June. Bookings rose a strong 3.4% in May.

UNEMPLOYMENT CLAIMS

Thursday, July 25, 8:30 a.m. EDT ► New filings for state unemployment benefits likely stood at about 340,000 for the week ended

July 20. Despite very tight labor markets and good job growth, jobless claims remain high. Filings jumped by 17,000 in the week ended July 6, a surprise gain considering state employment offices were closed on Independence Day.

EXISTING-HOME SALES

Thursday, July 25, 10 a.m. EDT ► Sales of existing homes probably fell to an annual rate of 4.16 million, says the MMS median projection. The housing sector has been resilient throughout 1996. Resales dropped only once this year, slipping 3.9% in January. In May, existing-home sales rose 1.4%, to a 4.26 million pace, the highest level in nearly three years.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (7/13) thous. of net tons	1,941	2,005#	0.8
AUTOS (7/13) units	50,646	11,904r#	26.8
TRUCKS (7/13) units	32,446	10,522r#	122.6
ELECTRIC POWER (7/13) millions of kilowatt-hrs.	70,594	69,553#	-5.1
CRUDE-OIL REFINING (7/13) thous. of bbl./day	14,147	14,160#	-2.7
COAL (7/6) thous. of net tons	13,554#	17,815	-14.1
PAPERBOARD (7/6) thous. of tons	883.7#	910.0r	-0.7
PAPER (7/6) thous. of tons	771.0#	800.0r	-7.4
LUMBER (7/6) millions of ft.	300.2#	474.0	29.2
RAIL FREIGHT (7/6) billions of ton-miles	21.3#	24.3	2.9

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPA1, SFP2, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (7/17) \$/troy oz.	383.400	383.000	-1.5
STEEL SCRAP (7/16) #1 heavy, \$/ton	133.50	133.50	-5.0
COPPER (7/13) ¢/lb.	93.7	92.5	-35.8
ALUMINUM (7/13) ¢/lb.	70.0	69.5	-19.5
COTTON (7/13) strict low middling 1-1/16 in, ¢/lb.	76.55	76.43	-20.3
OIL (7/16) \$/bbl.	22.24	21.30	28.3

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (7/17)	108.66	110.08	87.48
GERMAN MARK (7/17)	1.49	1.52	1.39
BRITISH POUND (7/17)	1.55	1.55	1.59
FRENCH FRANC (7/17)	5.03	5.16	4.82
ITALIAN LIRA (7/17)	1522.0	1534.3	1604.4
CANADIAN DOLLAR (7/17)	1.37	1.37	1.36
MEXICAN PESO (7/17)	7.648	7.611	6.140

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

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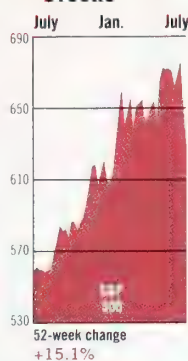
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Investment Figures of the Week

STOCKS

Markets were slammed this week, though interest rates retreated in the wake of good numbers on the front. For the week, the industrials were down an average 4.0%, about the same as the decline in the Nasdaq. The new high on Wall Street: earnings. Pity the company whose earnings came in below what analysts were expecting. Disappointments in such large stocks as Hewlett-Packard and HealthCare sent their stocks falling more than 10%. The rally in high-tech stocks reported for earnings was a lot worse.

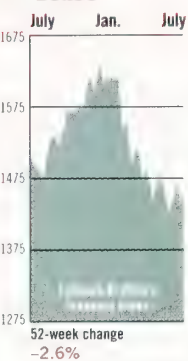
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
INDUSTRIALS	5376.9	-4.0	16.2
TECH COMPANIES (S&P MidCap Index)	220.2	-3.8	10.7
COMPANIES (Russell 2000)	318.2	-4.4	10.8
COMPANIES (Russell 3000)	359.6	-3.5	14.6

IGN STOCKS	Latest	% change (local currency) Week	% change 52-week
N (FINANCIAL TIMES 100)	3658.2	-2.9	7.4
(NIKKEI INDEX)	21,412.9	-1.7	30.4
TO (TSE COMPOSITE)	4940.0	-3.1	7.2

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.26%	5.27%	5.55%
30-YEAR TREASURY BOND YIELD	7.03%	7.08%	6.51%
S&P 500 DIVIDEND YIELD	2.26%	2.19%	2.45%
S&P 500 PRICE/EARNINGS RATIO	18.7	18.9	16.8

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	634.1	656.1 r	Positive
Stocks above 200-day moving average	39.0%	55.0 %r	Positive
Speculative sentiment: Put/call ratio	0.89	0.72 r	Positive
Insider sentiment: Vickers sell/buy ratio	2.26	2.57	Neutral

INDUSTRY GROUPS

MONTH LEADERS	% change 1-month	% change 12-month	Strongest stock in group	% change 1-month	% change 12-month	Price
OIL AND GAS DRILLING	16.1	73.6	ROWAN COMPANIES	19.6	127.1	16 ¹ / ₄
EXPLORATION AND PRODUCTION	9.5	15.1	BURLINGTON RESOURCES	11.9	16.7	44 ¹ / ₂
MINERAL GAS	4.9	29.9	COLUMBIA GAS SYSTEM	12.7	60.4	52 ¹ / ₂
WELL EQUIPMENT AND SERVICES	4.8	33.6	BAKER HUGHES	10.0	54.7	32 ¹ / ₂
ELECTRIC COMPANIES	2.2	4.9	TEXAS UTILITIES	6.9	25.7	42 ³ / ₄

MONTH LAGGARDS	% change 1-month	% change 12-month	Weakest stock in group	% change 1-month	% change 12-month	Price
PACKAGING	-31.3	-42.2	CALIBER SYSTEM	-41.0	-50.9	21 ³ / ₄
OS	-22.5	-3.1	UNITED HEALTHCARE	-38.5	-30.2	32 ¹ / ₂
MACHINE TOOLS	-22.2	-37.8	GIDDINGS & LEWIS	-32.1	-38.6	11 ¹ / ₂
'S	-19.1	3.6	MATTEL	-21.0	4.4	22 ¹ / ₂
BROADCASTING	-16.3	-16.8	TELE-COMMUNICATIONS	-19.0	-20.8	14 ¹ / ₂

MUTUAL FUNDS

LEADERS		LAGGARDS	
4-week total return	%	4-week total return	%
ELITY SELECT NATURAL GAS	9.2	PREMIER STRATEGIC GROWTH A	-22.4
ELITY SELECT ENERGY SERVICE	7.8	JUNDT U.S. EMERGING GROWTH C	-19.3
ELSIOR LONG-TERM SUPPLY OF ENERGY	6.7	DEAN WITTER HEALTH SCIENCES	-17.7
52-week total return	%	52-week total return	%
MARK SMALL CAP EQUITY A	77.2	STEADMAN TECHNOLOGY GROWTH	-35.9
NITREND GOLD	48.4	STEADMAN AMERICAN INDUSTRY	-29.5
EMONT U.S. MICRO-CAP	48.3	SELIGMAN COMMUNICATIONS & INFORM. D.	-24.2

S&P 500

Average fund

4-week total return

</

RELATIVE PORTFOLIOS

Amounts represent the net value of \$10,000 invested one year ago in each portfolio	U.S. stocks	Foreign stocks	Money market fund	Gold	Treasury bonds
Percentages indicate daily total returns	\$11,599 -4.03%	\$10,945 -1.09%	\$10,530 +0.11%	\$10,148 +0.72%	\$10,119 +1.49%

Data on this page are as of market close Wednesday, July 17, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close July 16. Mutual fund returns are as of July 12. Relative portfolios are valued as of July 16. A more detailed explanation of this page is available on request. r=revised

RIDE OUT THE ROLLER COASTER

Investors can be forgiven if they have a queasy feeling in their stomachs. Since early July, the stock market has lost 6% of its value, culminating in a sharp plunge and recovery on July 16. Such volatility, rarely seen in the past five years, is likely to be more common in the months to come.

Faced with such a market, it is critical for America's economic health that investors and corporations maintain a long-term investment strategy. Many of the economic woes in the 1980s were the result of shortsighted decisions. Companies managed for the next quarter, abandoning markets at home and abroad to foreign rivals rather than investing for the future. Money managers, pushing for quick gains, supported this short-term view. But in the 1990s, things seemed to have changed. Companies have stepped up spending on new equipment and, in some cases, have been willing to give up short-term profits for long-run advantage. Baby boomers, worried about retirement, are finally thinking long-term and pouring enormous sums into mutual funds through their 401(k) plans. Small investors, confounding most experts, have continued buying stocks even when the market dipped.

A long-term perspective is easy to maintain while markets are rising steadily. But it's far harder to be patient when the market is swinging widely. Small investors with retirement funds at stake will have to learn to stick out the inevitable declines. Economic studies suggest that the average investor has a time horizon of about a year—but that won't be enough.

U.S. companies now have a chance to show their commitment to long-term innovation, investment, and planning. In recent years, soaring markets have made it cheap for companies—especially small startups—to raise funds for spending and expansion. Perhaps they will now have to pay more for their capital. But if the U.S. is serious about competing over the long term, business must be willing to keep investing.

GETTING TOUGH ON SWEATSHOPS

Out of sight, out of mind? Not in the clothing industry. Once, Americans had little idea where imported shirts, shoes, and dresses came from. But better communication means that garment shops in Indonesia or Honduras are now on the other side of the TV screen rather than the other side of the world. Companies such as Nike are under attack for tolerating deplorable working conditions and low wages in their own overseas factories and those of their suppliers.

Let's get one thing straight: These corporations are not oppressing the workers of developing countries by hiring them. The success of Taiwan and Korea has shown that exporting to global markets is a smart strategy for economic develop-

ment. Moreover, the production techniques and organizational knowledge brought by foreign investment can have a positive spillover effect for the rest of the economy.

But global companies can no longer afford to close their eyes to the conditions in the factories where their products—and profits—are made. As the recent uproar against Kathie Lee Gifford reveals, American consumers can sometimes react strongly against products perceived as made by "sweatshop labor."

Corporations that depend on suppliers in developing countries should follow such pioneers as Levi Strauss and Gap. These companies have learned from experience to monitor labor practices of their subcontractors, with an eye to preventing the worst abuses. Operating in poor countries also need investment and jobs, global companies have enormous leverage to push for improved working conditions and wages. Such pressure has its limits, since competition in the global apparel industry is fierce, and clothing prices have been declining for years. But it's the right—and profitable—thing to do.

A NO-PORK DIET FOR WASHINGTON

The budget deficit is shrinking: The Clinton Administration, using figures from the Office of Management and Budget, predicts the shortfall for fiscal 1996 will come in at \$117 billion, or \$29 billion below forecast. But the good news disguises a disappointing trend. It's turning out to be harder than expected to cut "corporate welfare"—expensive subsidies and tax breaks such as gasohol supports and the Agriculture Dept.'s underwriting of overseas advertisements for agribusiness giants. According to a new study from the Cato Institute, Congress and the President managed to cut less than \$3 billion, or 14%, of the \$19.5 billion annual cost of the 35 largest corporate-subsidy programs.

Now it's time to try a new way to cut corporate subsidies. A proposal by Senator John McCain (R-Ariz.) would set up a federal commission to take on corporate welfare. It would be modeled on the military base-closing commission, which has successfully eliminated superfluous bases across the country that had previously been politically untouchable. Rather than trying to isolate and kill individual programs, the panel would spend a year putting together a list of subsidies and loopholes to cut. Congress and the President would then have to accept or reject the entire package.

McCain's idea has its flaws. Congressional supporters often want to ensure that basic research isn't tossed out along with corporate welfare. And the need for an unelected commission confirms the lack of political leadership. But subsidies and tax breaks that benefit specific companies and industries are bad for business and bad for the economy—just as they are bad for the budget. Both parties agree that corporate welfare has to go. The pork-busting commission is one piece of legislation Congress must pass before its members go home to boast about their budget-cutting credentials.

August 4

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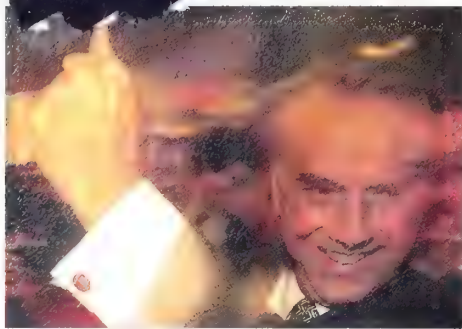
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IT'S A PLACE CALLED THE INTRANET.

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As V.P. and resident visionary for QUALCOMM—one of the brightest stars in digital wireless communications—Tom Lafleur is finding innovative ways to stay ahead of his company's phenomenal growth with the help of the World Wide Web and Apple Macintosh computers. In fact, Tom started QUALCOMM's Intranet by running one of their own products on a Mac—Eudora, which has since become the most popular e-mail software for the Net. Today, people are using Macintosh to easily create web pages and share details of their projects with the rest of the organization. So engineers have instant insight into manufacturing problems, can pull up drawings and quickly resolve issues. Which has slashed the need for paper. Cut support costs. And sparked unprecedented collaboration. Not to mention knocking a few walls down along the way.





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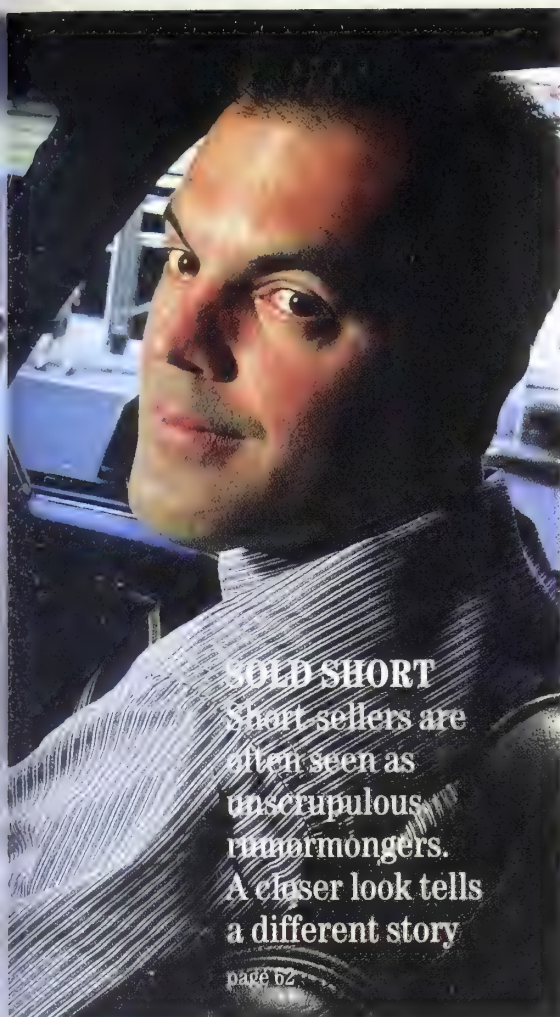
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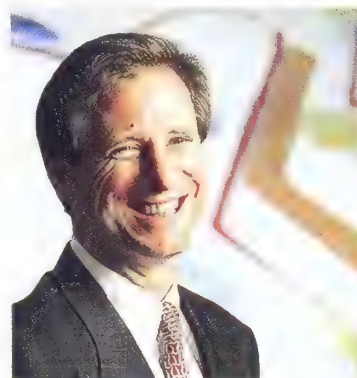
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Get back to the budget, guys
Mandate bomb scanners now
Don't sell the shorts short

Up Front

EDITED BY LARRY LIGHT



ADM'S ANDREAS: *Reforms?*

PROXY MOXIE

DEAR SEC: IGNORE OUR SHAREHOLDERS

ARCHER DANIELS MIDLAND, which pleased institutional investors by revamping its board, now is asking the SEC to derail four big investors' proposed reforms. To their outrage, ADM seeks approval to omit three of their proposals from the October annual meeting's proxy statement.

Just recently, the share-

holders were welcoming ADM's efforts to overhaul the 17-member board they considered too close to Chairman Dwayne Andreas. This spring, the agribusiness giant—under federal investigation for alleged price-fixing—said it would remove executive directors, other than Andreas, and appoint three outside members. A good start but not enough, say the four investors, who represent 10 million shares.

The California Public Employee Retirement System and the Florida Retirement System Trust Fund both call for a majority of independent directors. The New York City Fire Dept. Pension Fund wants confidential voting for directors. The United Brotherhood of Carpenters Pension Fund wants to hold directors liable for "gross negligence."

ADM calls its SEC move "an ordinary legal step," and hopes to work a deal with investors. *Richard Melcher*

SHOW BIZ

A RENT STRIKE IN HOLLYWOOD?



A HIT! *On the stage, at least*

BIDDING FOR MOVIE RIGHTS to Broadway's *Rent* has its share of drama, too. Bidders have dwindled, with Danny DeVito's Jersey Films the latest to quit. But sources close to the action say *Rent* will still bag up to \$5 million, a lot in a time when movie musicals aren't common.

Why have four of eight bidders split since April? Maybe it's the pickiness of the sellers: the late playwright Jonathan Larson's family, which won't comment. It fears a movie of *Rent*, set among artsy East Village vagabonds, won't be true to his vision. It vetoed Peter Guber's Mandalay Entertainment, concerned his *Rent* would be too Hollywood, a source says. Mandalay says bidding got too high, so it quit.

The auction has dismayed several studios. "It's not a gift certificate redeemable whenever they want it," says a Hollywood executive bidding for *Rent*. Now, some production outfits aren't sure *Rent* is mainstream enough. Still in the game: 20th Century Fox, Warner Bros., New Line, and Robert De Niro's Tribeca. *Andrew Ross Sorkin*

TALK SHOW "I would only say to anybody else who has a birthday today, 'Happy birthday. You can have mine.'"

—Bob Dole, upon turning 73 on July 22

MUNI MADNESS

UNCLE SAM MAY PLAY SCROOGE WITH BONDS

THE FEDS MIGHT MAKE YOUR nice tax-exempt muni taxable next year. This stems from the IRS's quest for money it says it's owed by municipal-bond issuers, such as states and towns. The IRS said in a



July 19 ruling if the municipalities don't cough up the money in a year, it may yank their paper's exemption. One estimate: \$1 billion is owed.

A big chunk of the muni universe may be at risk: \$1 billion in bonds issued since 1989 (of a total \$1.2 trillion). The issuers say they're not to blame and point to their Wall Street underwriters. The IRS centers on the practices of municipalities taking funds raised by muni sales and investing it temporarily in Treasury securities. But in some cases, the feds suspect underwriters overcharged for the Treasuries—thus the money the IRS seeks. To date, the IRS hasn't publicly named any firms.

By threatening to yank the tax exemption of muni bonds, the IRS is apparently pressuring the issuers to get the money from the Wall Street firms. The feds believe that the issuers will be successful, so bondholders won't be hurt. *Leah Nathans Sp*

FAT WALLETS

NOT EXACTLY A DAY'S PAY FOR A DAY'S WORK

WHO ARE THE MOST OVERPAID and underpaid chieftains of midsize companies? According to pay expert Graef Crystal, the overpaid award goes to Linda Wachner of Warnaco Group, which last year paid her \$16.6 million.

By Crystal's formula, which factors in company performance and size, Warnaco (1995 sales: \$916 million) overpaid Wachner 892% last year. He estimates a "competitive level of pay" for her would have been \$1.7 million. Earnings were down 21% in 1995. Although Warnaco rebounded in 1996's first quarter, Wachner, 50, warns that a huge charge to

close plants and discontinue Hathaway shirts will sock second-period profits. The company says her pay is justified by its growth during her 8-year tenure.

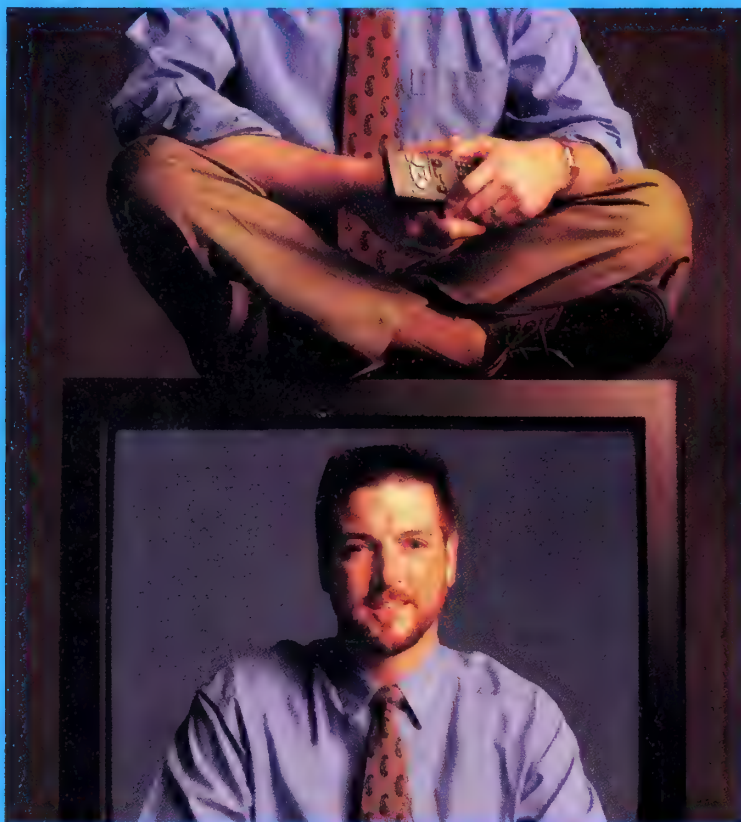


WACHNER: *Paid \$16.6 million in '95*

The most underpaid? Dan Terra, the 46-year-old founder of specialty chemical maker Lawter International. Lawter (\$204 million in sales) had four times, too—profits slid 44% last year. But Terra got a salary or bonus of \$1.7 million. Terra, who did

June 28 at 85 after a heart attack, waived his \$450,000 pay, which he had done since 1982. Crystal figures competitive pay for him would have been \$316,000. *John Byrne*

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Tim Badger, Senior Test Engineer
Philips Broadband Networks, Inc., Manlius, NY



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PHILIPS

Up Front

HUNTING HEADS

SMILE, YOU'RE ON JOB-CANDIDATE CAMERA

FORGET ABOUT GOOD TABLE manners and a firm handshake. High on executive recruiters' lists for top-level job seekers these days: screen presence.

Videoconferencing is now a popular screening tool at large and small search firms, including Korn/Ferry International, Christian & Timbers, and Boston-based Fenwick Partners. Recruiters often videoconference for an initial meeting because "clients want cheaper, shorter searches,"

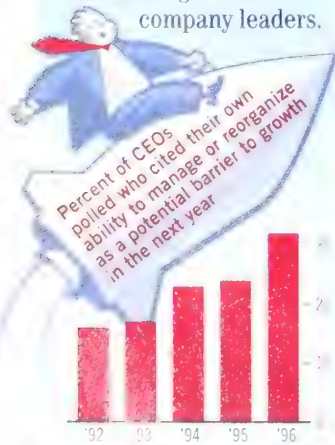
says Windle Priem, North American president of Korn/Ferry International. A partnership with copier service Kinko's, which has video conferencing facilities worldwide, allows Korn/Ferry to connect with candidates in such far-flung locales as Seoul. Domestically, fees start at \$150 per hour. Fenwick Partners' digital interviews are so frequent that it's installing a \$35,000 Picturetel system in its offices.

Still, there are drawbacks. Talk can be stilted, since two voices can't be heard simultaneously. Body language isn't discernible. "One guy wowed us onscreen but blew it in person. His shirttails hung out, and his shoes weren't shined," says Christian & Timbers' CEO Jeffrey Christian. And the camera isn't always kind: "My face looks like a pumpkin onscreen," admits Lamalie Anprop International recruiter Glenn Anderson. *Lisa Sanders*

THE BIG PICTURE

GROWTH GETS HARDER TO MANAGE

Nearly 800% revenue growth in the past five years looks great on the bottom line. But the demands of expansion—entering foreign markets, managing technology, and finding skilled workers—are getting more intimidating for small-company leaders.

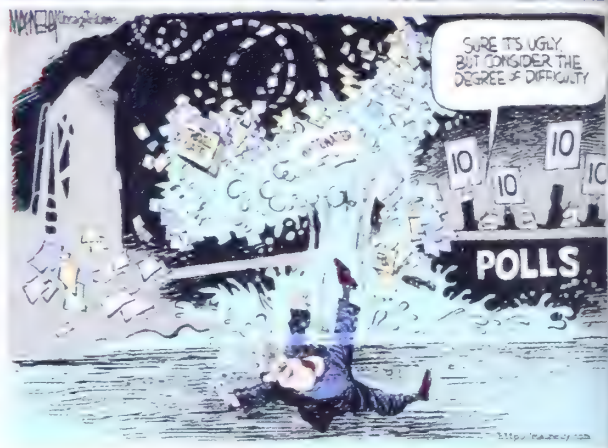


SILICON SAGAS

APPLE COULD LEARN AT ITS CLONE'S FEET

THE FASTEST MACS IN THE land are here. And they aren't made by Apple. Power Computing outside Austin, Tex., the only significant Mac cloner to date, began shipping a superfast PC, its fully loaded PowerTower Pro, based on a 225-megahertz PowerPC chip, on July 22. And in early August, Power will announce home Macs for the masses with speeds of up to 240 Mhz—well above Intel's current 200-Mhz best.

DRAWN & QUARTERED



AFTERLIVES

A PLEA FOR KINDER, GENTLER POLS

EX-HOUSE SPEAKER Jim Wright knows all about thorny encounters. These days, the worst involve rose bushes in his Fort Worth yard—far less painful than his 1989 ouster from power due to an ethics complaint filed by nemesis Newt Gingrich.

Although he has left the confines of the Beltway, the 73-year-old Democrat hasn't abandoned politics. Wright teaches political science at Texas Christian University, writes commentary for the *Fort Worth Star-Telegram*, and with former President Jimmy

Carter has monitored elections in Haiti, Nicaragua, and Panama. Despite an apparently successful battle with melanoma cancer, he has also authored two recent books.



WRIGHT: Writing

Tours to promote his latest, *Balance of Power: Presidents of Congress from the Era of McCarthy to the Age of Gingrich*, keep him abreast of voter sentiment. People, Wright says, "fear that the Republican House leadership is mean-spirited, petulant, and self-centered." He dislikes the current "politics of personal destruction" although no fan of Gingrich, admits to feeling some sympathy for the House Speakers he's roasted by the Democrats. *Richard S. Dunbar*

So is Power, a private company that says it has been profitable since mid-'95, gloating at Apple's expense?

Nope. It's publicly and loudly rooting for



struggling Apple's survival. While Power is small enough to prosper for a year or two, ultimately it needs the Mac platform to

thrive. At the upcoming MacWorld trade show in Boston, Power will set up a 225-foot bungee cord where Mac lovers can leap from a platform. They'll have a huge banner that reads: "Let's fight back for the Mac."

Maybe Apple CEO Steve Amelio can learn something from Power's chief, Stephen Kahng. Power works closely with IBM's chip division on its newest machines and is ready to exploit the latest chips. Plus, Power, with 40 employees, has paid top dollar to raid techies from Gateway and Dell—not to mention Apple, whose brain drain is a big problem. *Peter Burrows*

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ETHICS STARTS AT THE TOP

I was disappointed in the cynical tone of "Ethics for hire" (News: Analysis & Commentary, July 15). While I agree that some corporations reactively seek a "quick fix" in response to costly ethics blunders, your article ignores thousands of businesses, often small or midsize, that proactively instill ethics into the decision-making process or nurture ethical behavior among employees.

Values such as integrity and honesty must be supported by company leaders and reinforced through the organization's reward systems.

James Weber
A.J. Palumbo School of
Business Administration
Duquesne University
Pittsburgh

Unless employees believe that those with decision-making authority "walk the walk" as well as "talk the talk" of ethics, even the best ethics policies will be difficult to integrate into the culture of the organization.

Steven M. Mintz
School of Business &
Public Administration
California State University
San Bernardino, Calif.

Companies wanting a truly independent investigation of internal wrongdoing with a level of credibility that the authors of "Ethics for hire" find lacking should hire an Independent Private Sector Inspector General (IPSIG). The brainchild of a group of public officials, attorneys, forensic accountants, and private investigators in the New York City area, the IPSIG is a multidisciplinary team that provides investigative, legal, auditing, monitoring, and loss-prevention services.

It reports its findings not only to the company but simultaneously to an independent entity, such as a government agency or special committee of outside directors. A strict code of

CORRECTIONS & CLARIFICATIONS

"A rich rack of paperbacks" (Books, July 8) wrongly said Calumet Farm Inc. was sold to a Brazilian breeder for \$12,000. The breeder purchased Calumet's colors only

In a July 29 correction, Ghirardelli Chocolate Co. was incorrectly described as the world's oldest chocolate company.

ethics governing the work of IPSIG guards against conflicts of interest and other integrity lapses that might interfere with a genuinely independent investigation.

Neil V. Gettle
President
International Association
of Independent Private
Sector Inspectors General
New York

Things that are legal are not necessarily ethical, for the law does not attempt to anticipate all conduct. What Corporate America needs are leaders for whom ethics—a sense of right and wrong, not of what's legal and illegal—is important.

Frank H. Stoy
Spokane, Wash.

THERE'S NOTHING 'MEDIocre' ABOUT ICN

As a member of the ICN Pharmaceuticals board, I would like to point out that you unfairly characterized the company's financial and operational status ("Milan Panic may be starting sweat," Finance, July 1). The article unfortunately sensationalized past allegations and branded ICN as "mediocre." This is not the case.

In the past few years, ICN has added to top management a significant number of scientists and business executives with international reputations for excellence. Record sales of \$508 million and a \$50 million reduction in debt by year, followed by record sales, earnings

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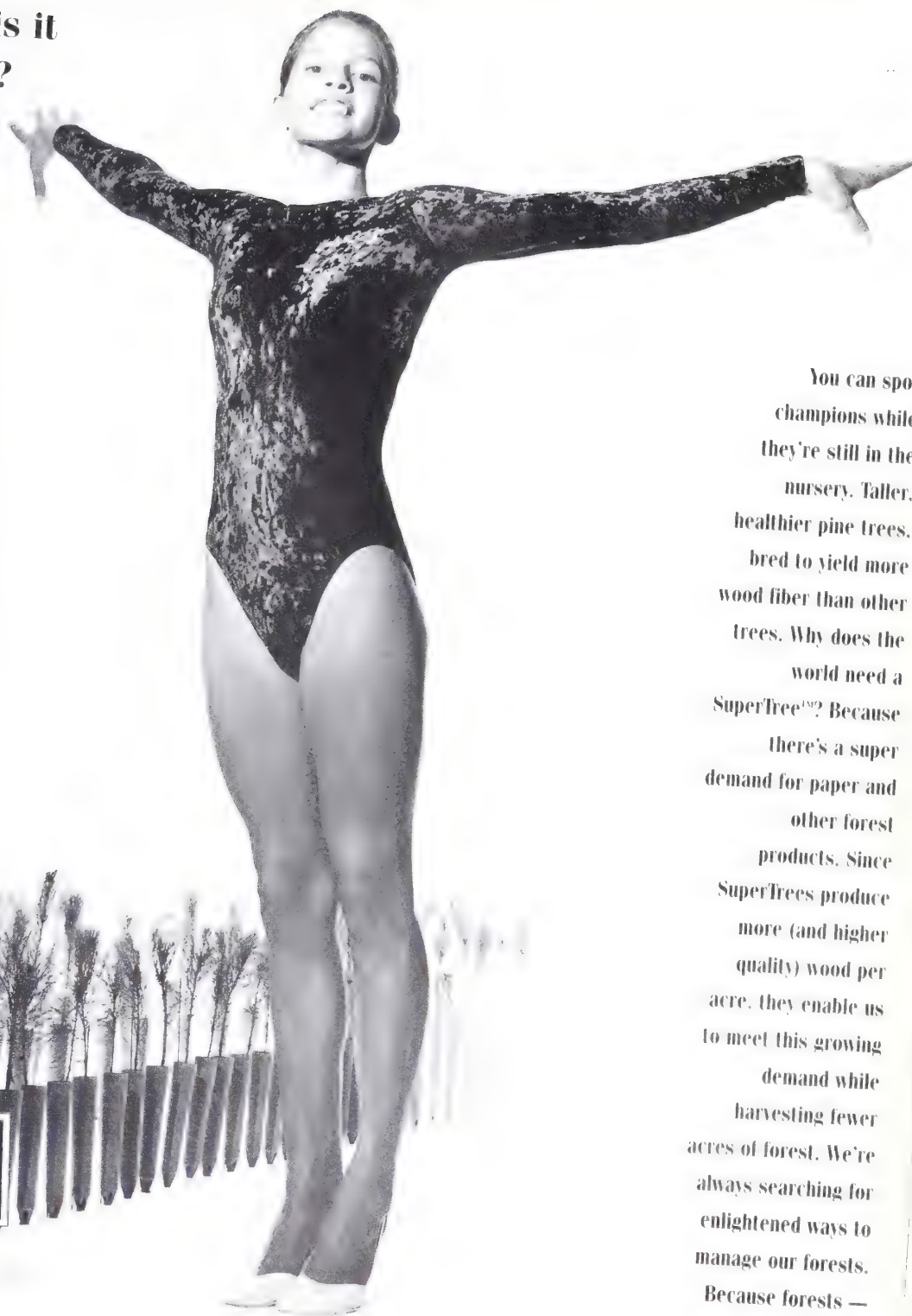
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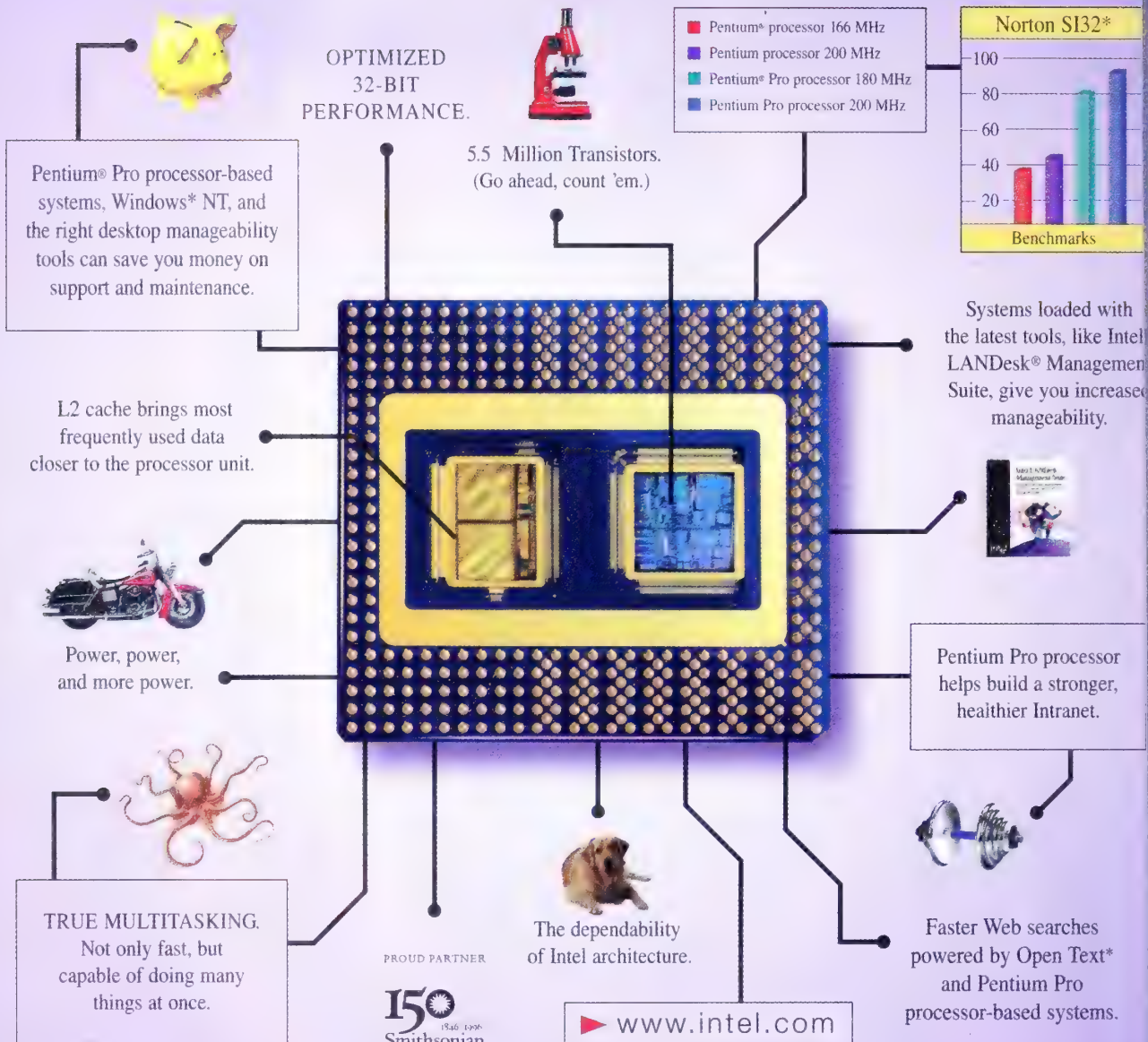


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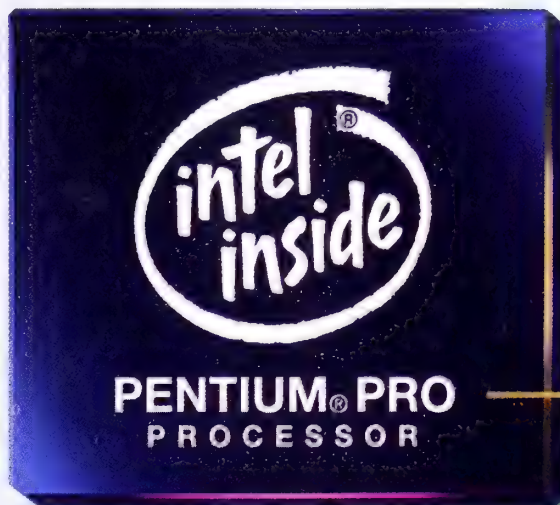
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Readers Report

net income in the first quarter of '96, are impressive by any measure.

Birch Bayh
Washington

REGULATION VS. SAFETY: THE CHOICE IS OBVIOUS

Howard Gleckman says: "The FAA is doing exactly what the public wants: Analysis and Commentary, July 15. Not so. The public was never asked whether it wanted to compromise in order to save a few dollars. The answer would have been resoundingly negative. Get bureaucrats off business' backs? Sure, but safety inspectors represent the public's legitimate interest in self-protection.

Thomas T. Semon
Demarest, N.J.

THE BILL GATES'S TROOPS MARCHING TOO HARD?

Bill Gates's strategy for dealing with the Internet has less to do with management skills and more to do with a rich running scared ("Inside Microsoft," Cover Story, July 15). If he didn't have

deep pockets—allowing him to throw money at problems he creates or opportunities he does not foresee—he couldn't play catch-up as he has.

Furthermore, hiring young people with the expectation that they will work excessive hours is not good management. Working at that pace leads to quality-control problems. People are not robots. People need time for rejuvenation. Perhaps Microsoft would not have missed the wave the first time if its people were encouraged to take time for community involvement and family responsibilities. People cannot be creative when they are exhausted.

Barbara E. Miller
Artemis Management Consultants
Mill Valley, Calif.

TERRORISTS CAN ALWAYS FIND A WAY IN

I have just read "Star Wars Junior: Will it fly?" (Science & Technology, July 15). It convinced me we will be able to guard against an ICBM launched by Iran, North Korea, or any of the other poor countries. But why would they try to beat us in a missile race? If they got their hands on nuclear devices, they

could float them into our ports. They could detonate them there or smuggle them inland on trucks. Either option would cause enough destruction to gladden the hearts of any set of fanatics.

Paul Ferrari
Edmonds, Wash.

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by Charles Mackay

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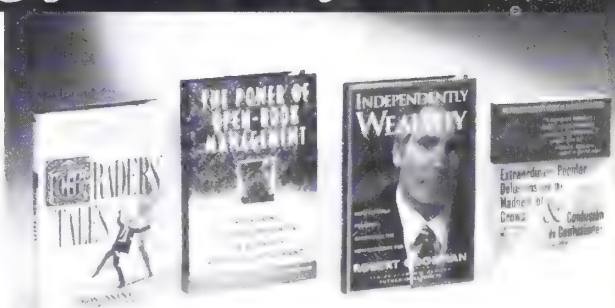
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IT'S ALIVE!

How America's Oldest Newspaper Cheated Death and Why It Matters

By Steven Cuozzo

Times Books • 342pp • \$25

NEW YORK POST TO REST OF PRESS: WISE UP

HEADLESS BODY IN TOPLESS BAR

The thick black letters screamed across the *New York Post's* front page on Apr. 15, 1983. It became perhaps the most famous, or infamous, headline in New York newspaper history. To most of the city's editors and writers, especially those at *The New York Times*, it was yet another affront to responsible journalism by press baron Rupert Murdoch, who had bought the paper in 1977. In 1980, the *Columbia Journalism Review* called the *Post* "a force for evil." But to the *Post's* staff, the headline was a triumph. "What should we have said?" asked *Post* editor Steve Dunleavy. "Decapitated cerebellum in tavern of ill repute?"

Well, times—and the *Times*—have changed. In *It's Alive!*, his "anecdotal memoir" of 24 years at the paper, Steven D. Cuozzo, the *Post's* executive editor, argues that the *Post's* "tabloid" journalism has fundamentally helped reshape the media—mainly for the good. The *Post's* emphasis on personality and its "gift for telling a human story colorfully and dramatically," he says, are now ubiquitous: Witness mainstream magazines such as *Vanity Fair* and *People*, TV shows such as Fox's *A Current Affair* and ABC's *Prime Time Live*, and the once-gray *Times* itself. Can we ever forget Diane Sawyer getting Marla Maples to tell us about her "best sex" with The Donald? As Cuozzo sees it, it was the *Post* that "broke the elitist media stranglehold on the national agenda."

As a chronicler of the *Post's* exploits and a passionate advocate of tabloid values, Cuozzo is in a somewhat compromised position. He signed a contract to write *It's Alive!* on Mar. 31, 1993, a time when it seemed certain the financially ailing *Post* would go under. But Murdoch, who sold it in 1988, returned

to rescue the paper. Cuozzo then told his book editor that he would take his account only up to the contract signing date. But the book contains an afterword that extends the narrative to the present. And Cuozzo continues to function as one of the top *Post* editors—giving him a strong motive to portray himself, his co-workers, the *Post*, its owner, and the whole of tabloid journalism itself in a favorable light.

Bearing that in mind, *It's Alive!* is still a lively romp through the *Post's* tumultuous recent times—starting in the early 1970s, when Cuozzo joined the paper. The parade of feuds, fights, firings, frolics, and fiascos makes *The Front Page* seem, by comparison, like a story meeting at *Biblical Archaeology Review*. And the *Post's* near-death experiences were almost annual events. The odd array of owners has included Peter S. Kalikow, a real estate magnate who went bankrupt, Steven Hoffenberg, a financier who pleaded guilty to securities fraud, and Abraham D. Hirschfeld, a true eccentric who made his fortune building parking garages. One day in 1993, when Hoffenberg and Hirschfeld were sharing *Post* ownership, the two got into such a fight that the former chased the latter down the hall. To protest the firing of four staff members, longtime on-and-off staffer Pete Hamill once edited the paper from a diner.

Cuozzo sees a role for both tabs and "trads": Each serves "as a philosophical check and balance on the other." But he criticizes the so-called responsible media for insisting that they rely "on 'balance' and a dispassionate tone [that] imply an objectivity and thoroughness." Meanwhile, such media brand the tabloids'

coverage as superficial, biased, and marginal. Cuozzo argues, not without reason, that mainstream media claim to the journalistic high ground "exist principally in the imagination of journalism professors." In fact, Cuozzo says, "there is no trouble finding every kind of error, misrepresentation, statistical gamesmanship, and exaggeration masquerading as fact" in the mainstream press.

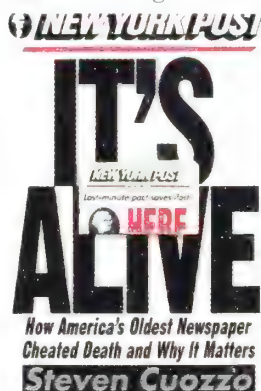
More telling, he faults the mainstream press for explaining events in terms of "underlying forces" like wars, economic upheavals, social change, and the activities of government and corporations—all of which imply the work of a "collective will." Cuozzo contends that events are more accurately explained in terms of "individual human passions." Among arguments—a quote from Alexander Hamilton, who founded the *Post* in 1785: "Has it not been found that momentary passions... have a more active and powerful control over human conduct than general or remote considerations of public utility or justice?"

Focusing on "individual and dramatic storytelling" as Cuozzo puts it, is probably the tabloids' most important contribution to news coverage. The newly personalized *New York Times* a few years ago ran a story on celebrity-kiss-and-tell author Kitty Kelley on page 1. And it pursued the William Kennedy Smith episode with a zeal that the *National Enquirer* might have envied. But even Cuozzo admits the personalization of news now often goes too far, as illustrated by the proliferation of trash TV and the blurring of news and entertainment.

Although Cuozzo sees the *Post* as the driving force in this trend, a claim that seems more than a little overblown, the paper itself is languishing, its readership largely eclipsed by the Establishment press. While the *Times* sells more than 1,158,000 copies daily, the *Post's* circulation has slumped from 700,000 in the late 1960s to 418,000 today. The paper lost \$20 million last year. In an age of O.J. and the Unabomber, *HEADLESS...TOPLESS* is strictly page 3.

BY CHRIS WELLS

Senior Editor Welles keeps tabs on the tabs.



CUOZZO ARGUES THAT TABLOID JOURNALISM HAS RESHAPED THE MEDIA—MAINLY FOR GOOD

GoldStar

WHY GO FOR
BRONZE OR SILVER
WHEN YOU CAN
REACH FOR GOLD?



LG Electronics
The future is making sense

Atlanta this summer 10,000 athletes are going for gold. And in over 170 countries around the world, millions of people are going for GoldStar.

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BY JACK PLUENNEKE

OLD NEWSHOUND, NEW WEB TRICKS

A high-tech agnostic learns to stop worrying and love the Internet

When I cleaned out my desk at BUSINESS WEEK 14 months ago to begin a long-term leave and finish a book, I was bombarded by warring emotions. My elation at the prospect of cybercommuting from a beachside cabin was dampened by the thought of cutting myself off from personal contacts and unlimited information resources.

The fretting was natural but needless. My need to stay plugged in coincided with the explosive growth of the Internet. My son, a committed cybernaut, had long preached the Internet gospel. But he had a problem: Pop was not a mere technological agnostic but a heretic of Luddite proportions. **COWPATHS.** In the end, it was like giving up cigarettes or following a diet: I just made up my mind. And here I am, one copy of Peter Kent's *The Complete Idiot's Guide to the Internet* (Alpha Books, \$19.95) later, surfing the Atlantic and the Net at the same time.

Who needs an umbilical cord when he has a modem? I use the Net to tap resources that seem without end. E-mail allows me to chat

with old friends and colleagues around the world easily and inexpensively. Online newspapers and magazines add a periodical room to my cabin. For fun, I take a break with sites about music, movie reviews, cars, and travel.

The Net also has the power to irritate. It can be frustratingly slow during periods of peak use. Inexplicable snafus can cause an instruction to abort a program. And the Net can disgorge mountains of junk. I learned that the Information Superhighway was a bewildering jumble of cowpaths. I needed a map. Fortunately, all the big search engines (Yahoo!, Alta-Vista, Lycos, et al.) and browsers have organized the Net into subject categories

How I Stay in Touch on the Net

THE WASHINGTON POST ONLINE

A terrific online version, with Net basics in plain English. <http://www.washingtonpost.com>

LEAD STORY The day's top story, bristling with informative links from AT&T.

<http://www.leadstory.com>

THE WALL STREET JOURNAL The full text of the paper, plus tons of market data. <http://www.wsj.com>

PERSONALIZED START PAGE Zoom to sites of your choice with links you choose in advance.

<http://www.msn.com>

IGUIDE Murdoch pulls out the stops with a brilliant Internet guide.

<http://www.iguide.com>

that I use to point me in the desired direction. Other indispensable guides are iGuide and the Net navigator in the CyberTimes section of the online *New York Times*—two of my favorite sites.

I've spent 40 years as a journalist, so I'm a news junkie. That's why the personalized start page I've programmed contains links to six news Web sites: the online versions of *The Washington Post* and *The Wall Street Journal*, AT&T's LeadStory, NBC's joint venture with Microsoft called MSNBC, Fox News on iGuide, and the ESPN sports coverage on SportsZone.

The online *Washington Post* dishes up the best coverage of the federal government, plus good coverage of Internet exploration equipment (browsers, earphones, and zippers—those programs that compress and decompress files for faster downloading). The online *Journal* is not just my starting point for financial information, it's

also the closest thing America has to a great national newspaper. Result: I spend a lot less time thumbing through newsprint. And since both papers are free online (for now), I save \$47 a month in the process.

I use the Website review in iGuide and the many links in LeadStory to surf with a specific subject. At MSNBC's dual versions on the Web and cable TV make more than just another pretty CNN-like face. I used the online incarnation's index to pick and choose material rather than shlep through the whole Web site.

NEW MIND-SET. Another road map to the news, used less frequently but still wonderful as a bookmarked backup is the Web site of the *American Journalism Review* (<http://www.newslink.org>). It provides links to 3,700 online newspapers, magazine broadcasters, and news services worldwide.

A special favorite is *Wire* magazine's online Hot-Wire, which demonstrates how the nature of the

Net fosters a very different mind-set. The linear thought processes of traditional journalism are out the window on the Internet, where the approach is peripheral. The viewer is constantly beckoned to wander off course by clicking on links in the form of icons, graphics, or hypertext. This scatterbrained characteristic of the Net drives some people nuts, but I find it one of its greatest charms. You could say that for this technology to come late, later thinking rules.

Pluenneke is BUSINESS WEEK special correspondent.



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MSNBC 24-HOUR NEWS

The Microsoft/NBC team hookup on the Net and the telly. <http://www.msnbc.com>

HOTWIRED Graphically and technically on the Net's leading edge. <http://www.hotwired.com>

SPORTSZONE ESPN's sweaty coverage of sports, plus lots of opinionated online features. <http://espnet.sportszone.com>



*Perhaps now, certain luxury cars
will start referring to themselves as the
Continental Airlines of automobiles.*

J.D. Power and Associates, a name synonymous with automotive excellence, has just awarded Continental the 1996 Frequent Flyer/J.D. Power and Associates Award as best airline for customer satisfaction for flights 500 miles and more. Quite an achievement, considering that only last year we ranked at the bottom. But we're not resting on our laurels. In the coming year, we will continue to do the things that we believe helped us reach the top. Like being among the best in the business at getting you and your baggage to your destination on time to all of our 180 worldwide destinations. Providing an award-winning frequent flyer program, OnePass.SM And improving our in-flight service to include such quality brands as Pete's Wicked[®] Summer Brew and Brothers[®] Foglifter Gourmet Coffee. In short, giving you more airline for your money. For reservations just call your travel agent or 1-800-523-FARE.

Continental 
More airline for your money.SM

Continental Airlines was the highest ranked airline for flights 500 miles and more in the Frequent Flyer/J.D. Power and Associates 1996 Domestic Airline Frequent Flyer Satisfaction Study.SM Study conducted among frequent airline travelers who completed 7,066 individual flight evaluations. © 1996 Continental Airlines, Inc.

BY RUDI DORNBUSCH

NEEDED: AN ABOUT-FACE AT THE TOP THREE CENTRAL BANKS



NEXT MOVE:
Japan and
Germany must
drop their
inflation
obsession and
spur growth.
By contrast,
the Fed
should start
tightening now

For the next few months, the performance of the world economy hangs on how monetary authorities in the top three economies handle the trade-off between growth and inflation. In Germany and Japan, the central banks must understand that the most immediate risk is renewed slowdown, not inflation. Central banks in Europe and Asia have for too long been obsessed with inflation. By contrast, in the U.S., with the unemployment rate at 5.3% and employment costs edging up, it's time for policy makers at the Federal Reserve Board to worry about overheating.

Barely a year ago, Japan was the weakest link in the world economy. It is just now emerging from a serious slump marked by price deflation. Last year's fiscal stimulus, the big drop in the value of the yen, and easy money all spurred recovery. Next, though, the government is planning a major consumption tax hike for early 1997. Moreover, aggressive restructuring by Japanese companies—investing offshore and bringing in imports—is under way. Unsurprisingly, business and consumer confidence remain fragile. Yet the Bank of Japan has begun to talk about the need to raise rates.

PRIME THE PUMP. The absence of inflation and rampant balance-sheet problems in Japan mean that monetary policy must stay easy. If the transition from fiscal stimulus to restraint does not get help from accommodating monetary policy, Japan's recovery will falter. Another slump or worse in Japan will hurt all of Asia—and thus deal a blow to a large chunk of the world economy.

Similar ripple effects could occur in Europe. There, the Bundesbank effectively runs monetary policy for all of Europe. In the aftermath of unification, the Buba did a great job in bringing inflation under control. That task is now accomplished—inflation is down to less than 2%—but the Buba keeps on waging the fight. The German economy is barely emerging from a recession. In fact, there is hardly a sign of recovery. Meanwhile, major fiscal tightening is scheduled across Europe as everybody undergoes the ritual cleansing required by the Maastricht treaty rules for monetary union.

Playing a hard-money strategy has served Germany well over the past few decades, and it is tempting to think it will forever be a good strategy. But that is not the case. Ger-

many has become too expensive, industrial dynamism is gone, unemployment is high and rising, and the welfare state is an unaffordable luxury—just as many German exports are luxuries to overseas buyers. The labor market is inflexible, with the cost of manufacturing labor at \$25 an hour against only \$15 in the U.S. Budget restraint will produce more unemployment unless interest rates are cut by one or two percentage points and the Deutschmark depreciates substantially against the dollar.

RECESSION FEARS. For the Fed, the policy problem is entirely different: The U.S. economy is at full employment, and more important, the first signs of renewed inflation have appeared in the employment cost index. This is the time for gentle monetary tightening to lock in the benefits of more than a decade of disinflation. It's true that inflation has never been called for tighter policies for some time, and it's fortunate that the Fed did not heed their advice, since it would have meant that millions of jobs would not have been created. But the latest growth spurt has brought with it a slight acceleration of inflation. Now is the time to bring the growth rate down to 2%.

Delay merely risks bringing back the old pattern of overexpansion followed by a sharp reversal with the risk of outright recession. Indeed, every recession in the postwar period was induced by the Fed. With prudent monetary policy—a correction toward slower growth just now—we can put aside the fear of recession and expect to cruise along indefinitely. The stock market correction, higher long-term rates, and an anticipated slowing in growth might do the trick. But the greater risk is that output isn't slowing enough to curb inflationary pressures, and that three months from now the Fed will have to scramble to tighten policy. Right now is a good time for the Fed to signal that it will not tolerate inflation higher than 3%—even if the stock market is weakening.

In Europe, central banks take inflation too seriously and understate the scope for monetary policy to help restore prosperity. They should take a lesson from the highly successful U.S. strategy of the past decade. In Japan, the central bank is plainly clueless; just looking at any undergraduate textbook will help. For the Fed, the challenge is biggest: Accepted that we have reached full employment and turn preemptively conservative.

Would you



MIND DYING

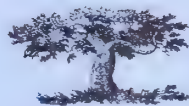
for a *moment*?

It's hard to imagine, but maybe you should take a few minutes to think the unthinkable. What would happen to your family? How would the mortgage be paid? Who would take care of the kids' college costs?

People with life insurance have the answer. It's there to ensure that the people you care about are provided for when you're not there to do it.

Whether you're a breadwinner or a homemaker, you're indispensable. So when you make financial plans for the future, think how life insurance could provide for your family if anything were to happen to you. Because life insurance isn't for the people who die, it's for the people who live.

A life insurance agent can give you a plan for life. A plan that makes sure the things you love will always be there for the people you love. Because no one plans to die, but everybody needs a plan for life. No one knows this better than your professional life insurance agent. Hundreds of people in your community trust an agent with their families' futures.



LIFESM

EVERYBODY NEEDS A PLAN FOR LIFE

BY GENE KORETZ

THE RIGORS OF POVERTY...

A new study details the hardships

To paraphrase F. Scott Fitzgerald's remark about the rich, the poor are different from you and me. Writing in the Labor Dept.'s *Monthly Labor Review*, a team of researchers uses survey data to detail many of the differences.

Although poverty is defined by income, the gap between the poor and others still seems stark. In 1993, the family income of the average poor person was \$8,500, roughly a sixth of the average income of other families. Welfare households averaged \$12,680.

While home-ownership rates among the poor and welfare recipients of 41% and 25%, respectively, seem high, it's important to note that the numbers are pushed up by high ownership among low-income elderly families. Similarly, the high rate of car ownership reflects the transportation needs of many poor working families.

More than 90% of the poor live in families with color TVs, refrigerators, and stoves, but nearly a quarter lack

higher infant mortality rates (chart).

Such statistics tell only part of the story. To measure the overall economic pressures felt by the poor, the researchers created an index based on such hardships as being evicted, having gas or electricity turned off, lacking food, living in crowded housing, and having no refrigerator, stove, or phone.

The final tally: In a typical year, some 55% of the poor and 65% of those in welfare families lived in households experiencing at least one such hardship, compared with 13% of the nonpoor. And 12% of poor and 15% of welfare families (but only 1% of the nonpoor) suffered at least three hardships.

...COULD BECOME HARSHER STILL

Welfare reform neglects downturns

Despite their good intentions, the welfare-reform bills currently before Congress could significantly increase the hardships suffered by America's poor during recessions. So concludes a recent analysis by economist Elizabeth T. Powers of the Federal Reserve Bank of Cleveland.

Powers notes that Congress' reform plans promise to save the states big bucks by ending unlimited entitlements to welfare. But the proposed reforms tend to ignore the sensitivity to the business cycle of such welfare programs as Medicaid, food stamps, and aid to the indigent elderly and to families with dependent children. Providing capped block grants to the states and only modest funds for emergencies, they would no longer oblige states to expand programs in times of high unemployment—just when work incentives are least likely to prove useful.

Yet history shows that welfare case-loads and outlays rise substantially during recessions. Powers' own "conservative" estimate, for example, indicates that a rise of one percentage point in unemployment in 1994 would have boosted annual outlays for major welfare programs by at least \$5.2 billion.

States could, of course, opt to spend more on welfare in hard times. But with new limits on federal support and new freedom to tighten standards and reduce benefits, they are more likely to cut back in the face of a recession-induced fiscal squeeze. The upshot could be tougher times for those in need—and less stimulus to stabilize the economy automatically during downturns.

ALL QUIET ON THE PRICE FRONT

Pressures are slack worldwide

The world economy may be picking up steam, but inflationary pressures are not. Indeed, the International Monetary Fund reports that global consumer prices, including the often volatile readings in developing countries, are about 8.6% over last year—the smallest rise since 1973 (chart).

Sluggish commodity prices are one reason. According to the IMF, non-commodity prices through May of this year were only 1.6% above 1995, as falling prices of metals, beverages, and other products offset soaring food prices.

Slower Asian growth and tighter economic policies in Latin America have cut inflation in developing nations. And in the world's industrial nations, where consumer prices are currently up only 2.5%, a combination of fiscal restraint, waning union power, a rising Asian import penetration promise to restrain inflationary pressures that may surface in the next year.

GLOBAL INFLATION IS IN REMISSION



HOW THE POOR FARE IN AMERICA

	NONPOOR FAMILIES	POOR FAMILIES	WELFARE FAMILIES
OWN HOME	77.6%	40.8%	24.9%
OWN CAR	97.2%	76.8%	66.3%
HAVE TELEPHONE	97.2%	76.7%	67.5%
TWO OR MORE PEOPLE PER ROOM	4.2%	19.2%	23.6%
VIOLENT CRIMES PER 1,000 PEOPLE	26.2	53.7	87.5*
INFANT MORTALITY PER 1,000 BIRTHS	8.3	13.5	14.3
NO HEALTH INSURANCE	13.0%	29.0%	18.0%*

Note: 1992-1993 survey data adjusted for family size
*Single-parent families (most of whom receive welfare)

SOURCE: MONTHLY LABOR REVIEW

access to a home phone. Less surprising are poor people's vulnerability to violent crime and reduced access to health care. Some 29% of the poor have no health insurance at all, compared with 13% of the nonpoor. More than 43% of poor mothers get inadequate prenatal care, compared with 16% of nonpoor mothers. Also, the poor suffer far

THE CLINTON MARKET RALLY?

History says it could be coming

Is the election cycle's impact on stock prices fading? Since 1941, notes Ma M. Groz of Quaternion Group Inc., consulting firm, total returns on stock in the S&P 500 in both the third and fourth years of Presidential terms have averaged in the double digits and have never been negative.

Judging by the recent market troubles, you may think this bullish streak about to end. But Groz spies hope for an upturn in the data. His analysis of monthly stock returns in the four years of the past 13 Presidential terms indicates that July has been by far the worst month, producing more declines than rises. Yet Groz points out that total returns in the second half of election years have always been positive.

JAMES C. COOPER & KATHLEEN MADIGAN

WILL GREENSPAN SEE INFLATION CLOUDS GATHERING?

U.S. ECONOMY "Well, Senator, you know, I think that the current period—meaning the early weeks of the third quarter—is a crucial period for this business cycle."

With those words to Senator Paul S. Sarbanes (D-Md.) during Chairman Alan Greenspan's semiannual report on monetary policy on July 18, the Federal Reserve chief kept the markets on alert. He suggested strongly that the prospect of an interest-rate hike rests with the upcoming economic data—all but saying that if the robust data doesn't settle down, we're gonna tighten.

Greenspan's testimony, which he repeated before a House subcommittee on July 23 without breaking new ground, was candid and unusually free of Fed-speak. He said that, while evidence of inflation pressures is scant, there are early indications that this episode of favorable inflation developments, especially with regard to labor markets, may be drawing to a close.

And even though the Fed is officially forecasting stronger growth and reduced inflationary pressures in the second half and into 1997 (table), the chairman noted

that any evidence of a slowdown was sorely lacking and that the process of slowing must become evident in the period immediately ahead.

That's why the Fed, which must act preemptively because policy works with a lag, has moved to a level of what Greenspan called "heightened surveillance." He said that the

coming weeks "will tell us to a substantial extent how the economy is likely to evolve, not only for the rest of the year but well into 1997."

BETWEEN NOW AND AUG. 20, the date of the Fed's next meeting, what will the Fed be looking for? Greenspan's testimony provided plenty of clues. A series of upcoming economic reports will form the basis for any Fed action—or inaction. They will all be released within four days of each other, so the period from July 30 to Aug. 2 could be one of high volatility in financial markets. Of course, there is no magic number that will push the Fed to move, but here's a general guide for what to look for in the data (table): The Labor Dept.'s employment-cost index (ECI), due July 30, will provide an important indication of inflation pressures. Greenspan mentioned in his testimony that the first-quarter acceleration in the wage compo-

nent of this index, to an annual rate of 4.6%, may be a sign that workers' willingness to surrender wage gains for job security may be lessening.

If the overall ECI for private-sector wages and benefits rises at a quarterly rate of 0.8% or more from the first quarter, and if the wage index does not settle down, then the Fed would read that data as evidence of emerging inflationary pressures. Right now, the median expectation among economists is 0.8%.

Wage pressures came to light in the monthly data in the June employment report. Greenspan, however, prefers the quarterly ECI measure of wages to the monthly numbers, since the ECI is not affected by the changing composition of employment. He noted that some of the recent pickup in monthly wages might be due simply to job shifts to higher-paying industries.

THE NEXT CRUCIAL ECONOMIC REPORT will come on Aug. 1 from the National Association of Purchasing Managers' reading on factory activity. Greenspan noted that perhaps the most important reason why the economy was not showing signs of slowing could be the desire of businesses to rebuild their inventories in the face of increasingly lean stockpiles. This would boost production and incomes heading into the second half.

Economists expect the NAPM's July index—a composite of orders, production, employment, inventories, and delivery times—to rise to 55%, up from 54.3% in June, suggesting accelerating activity. But the Fed will focus on two components of the report: the percentage of companies reporting slower delivery times and the portion paying higher prices for supplies.

The Fed chief said that mounting delivery delays in June raise warning flags that factory activity is picking up steam. If the NAPM's supplier-deliveries index rises to 55%, the third gain in a row, the Fed would view it as a sign that market slack is spent and that pricing pressures are rising. A confirming sign would be a rise in the NAPM's price index to 55%.

The most critical data, though, will come from the July employment report on Aug. 2. That will be the first

A FED'S-EYE VIEW OF THE ECONOMY

CENTRAL TENDENCY PROJECTIONS	
1996	1997
2.5–2.75%	1.75–2.25%
3–3.25%	2.75–3%
LESS about 5.5%	5.5–5.75%

DATA: FEDERAL RESERVE

THE NUMBERS THAT WILL CAUSE THE FED TO TIGHTEN

REPORT	FED WILL DATE HIKE RATES IF:
EMPLOYMENT COST INDEX	7/30 Up 0.8% or more
PURCHASING MANAGERS' REPORT	8/1
► SUPPLIER DELIVERIES INDEX	55% or greater
► PRICES PAID INDEX	55% or greater
EMPLOYMENT 8/2 REPORT	
► PAYROLLS	Up 220,000 or more
► JOBLESS RATE	5.3% or less
► HOURLY EARNINGS	Up 0.4% or more

DATA: BUSINESS WEEK

broad reading of the economy in the second half. Where the Fed is concerned, job growth must slow from its first-half pace of 232,000 per month, because at that pace, the jobless rate will reach 5% by yearend, an inflationary level by any economist's reckoning.

Analysts don't expect much slowing, however. The current expectation for payrolls is a gain of 200,000. Any increase will get a temporary boost from the Olympic Games, but a gain of 220,000 or more would probably be too hot for the Fed's taste. The central bank is already getting uncomfortable with the current jobless rate of 5.3% amid faster rising wages.

Finally, if July hourly earnings rise 0.4% or more, then yearly wage growth will increase to 3.5%, the fastest pace in 6½ years. Even a 0.3% gain would imply no slowdown from June's 3.4% pace. Given policymakers' growing concern with tight labor markets, a universally strong job report would make a *prima facie* case for a rate hike, maybe even before the Aug. 20 meeting.

THE FED WILL ALSO LOOK AT the second-quarter report on gross domestic product, due on Aug. 1. That reading is already widely expected to be strong—about 4% by current projections—so it's largely old news.

Still, there could be some forward-looking information in the mix of the components, especially between final demand and inventories. Overall demand appears to have held up well, led by consumer spending and hous-

ing. Labor market strength is offsetting the downward pressure from higher long-term interest rates and debt.

But as Greenspan noted, the stronger dollar is exerting some anti-inflation pressures, as it holds down import prices and diverts some of that strong domestic demand toward imports. Indeed, nonoil import prices fell for the second month in a row in June, and rising imports widened the trade deficit in May, to \$10.9 billion, up from \$9.6 billion in April. The wider trade gap was a big drag on second-quarter GDP (chart).

Looking ahead, Greenspan also pointed out that foreign economies are starting to pick up. Exports, which hit a record in May, will rise further in the second half, adding more fuel to manufacturing.

For a data hound like Greenspan, the coming weeks will provide a flock of economic leads to sniff out. Judging by his testimony, he seems genuinely uncertain about where the economy is heading right now. But his words also strongly suggest that his instincts are telling him that the risks of future inflation are on the rise. Based on the recent trends in the data, the numbers due out over the next week or so are likely to prove that his instincts are correct.

THE TRADE GAP STARTS TO YAWN AGAIN



ARGENTINA

FINALLY GETTING OFF THE GROUND

Evidence of Argentina's recovery keeps mounting, but not fast enough to please the financial markets—or improve the outlook for deficit cutting.

The strongest news came from the Latin American Economic Research Foundation (FIEL), which reported a 4.1% rise in industrial output in the year ended in the second quarter (chart). A June survey of manufacturers showed increased optimism about demand. In addition, construction—a major source of jobs—is expected to increase 15% in the second half, according to the Argentine Chamber of Builders.

Although real gross domestic product likely fell in the first

quarter, the government is still forecasting real GDP growth of 5% for the year. Private economists, though, see a more moderate 2.5%-to-3% pace, after real GDP fell 4.4% in 1995. Disappointed by the economy's slack growth and buffeted by recent volatility in the U.S. markets, the Argentine stock market has moved sideways since May.

Last year's recession did cut Argentina's inflation. Compared with year ago levels, consumer

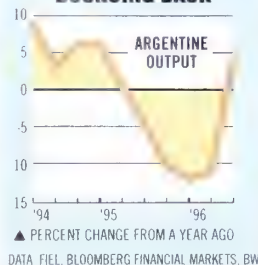
prices have fallen for the past three months, and inflation is expected to finish 1996 at just 2%.

One reason for the recent good news on the economy was a March cut in some value-added

taxes. But the government deficit was higher than expected in the first half and will likely overshoot its 1996 target of \$2.5 billion. As a result, the government of President Carlos Menem had to admit that Argentina will probably miss the fiscal targets set by the International Monetary Fund.

So on July 12, the government announced measures to increase taxes and cut subsidies, including an \$800 million reduction in child subsidies and abolition of some food vouchers. But those moves will hit the struggling consumer sector, whose spending is already expected to grow only 2% this year. Unemployment rose unexpectedly in May, to 17.1%, up from 16.4% last October. Unfortunately, modest growth will do little to lower either unemployment or the deficit.

INDUSTRY IS BOUNCING BACK



Now that your company is more lean, who can *you* lean on?

Do you have a minute? Probably not. But read on anyway. Because Kinko's can help you shed a few hats with Kinko's



do best. They'll work with you to learn your business. Your Account Manager will study how your company produces and uses

Corporate—an array of products and services that meet the stringent needs of our corporate customers. It's a new way for your company to tap Kinko's 25 years of expertise and our high-tech document reproduction capabilities. But perhaps the best feature of Kinko's Corporate is the Account Manager—someone to turn to for outsourcing so you can focus on the things you

printed material, and analyze the costs. Then they'll offer efficient, economical solutions for producing everything from thousands of pricing plans to sales manuals to quarterly reports. They'll even arrange pick-up and delivery. ♪ A Kinko's Account Manager is the extra muscle that a lean company needs. Which may be why more than 200,000 businesses use Kinko's every day.

The new way to office.™

kinko's
corporate

FOR MORE INFORMATION, PLEASE CALL 1-800-2-KINKOS FOR OUR BROCHURE.

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The deficit hawk recasts himself as a tax cutter. Why it may not work

If Republicans have one core belief left from the Age of Reagan, it's this: When they embrace tax cuts, they win elections. Bob Dole is staking the hopes of his fitful and floundering campaign for President on that abiding faith. After months of hesitation, Dole will embrace a massive cut in individual income taxes as the centerpiece of his economic agenda. By wrapping himself in Reagan's mantle, the lifelong deficit hawk hopes to transform himself and appeal to voters weary of a slow-growth economy.

This time, the GOP's tax magic might not work.

Dole's tax plan doesn't seem likely to deliver either the economic boost or the political help he needs. The growth GOP partisans claim will gush from lower tax rates is more likely to be a trickle, say most forecasters. And the candidate will have a hard time explaining how he'll cut taxes by as much as \$600 billion while finding almost \$1 trillion in spending cuts to balance the budget by 2002. Politically, Dole's dual promises are likely to remind voters of the Republican Congress' unpopular attempt last year to finance tax cuts with savings from Medicare. Polls show that voters would rather keep President Bill Clinton, who promises small, targeted tax cuts, in charge of fiscal policy.

SIMPLIFYING TAXES. The public's seeming defection isn't keeping Dole from throwing in his lot with the GOP's supply-side wing. Aides to the former Senate majority leader have been talking up tax cuts to rejuvenate his campaign since May. But Dole, who has a long career of backing tax hikes to cut the deficit, wavered. Then, on July 23, faced with a challenge from GOP leaders in Congress, he bowed, sending his chief policy adviser, Donald Rumsfeld, and his favorite deficit hawk, Senator Pete V. Domenici (R-N.M.), to a tax-cutting pep rally. Even Domenici declared that "we must reduce taxes on the American people."

Dole's blessing clears the way for advisers to move into final drafting of an economic agenda, which he'll unveil before



TAXES

DOLE PLAYS THE TAX CARD

MINDFUL OF THE DEFICIT, DOLE IS MULLING SEVERAL TAX CUT OPTIONS

ACROSS-THE-BOARD cuts in individual tax rates of 10% to 20%. Most likely: A 15% cut phased in over three years. **COST:** \$470 billion over five years.

ROLL BACK the 1990 and 1993 tax increases passed to reduce deficits under Presidents Bush and Clinton. To accomplish that, Dole is considering replacing today's five tax brackets with just two rates, 15% and 28%. **COST:** \$410 billion over five years.

FEDERAL BUDGET DEFICIT

Under current tax and spending policies

DATA: OFFICE OF

ELECTION '96

the Aug. 12 GOP convention. The package calls for such growth-boosting policies as cuts in regulation, product-liability reform to pare business' legal burdens, and school choice and vouchers to bolster education. He is also backing a list of tax breaks from last year's GOP Congress: estate tax relief, a broader home-office deduction, and cuts in the capital gains tax rate.

But the centerpiece of Dole's plan will be a sweeping cut in individual taxes, totaling more than \$400 billion over five years. The two main options: an across-the-board cut in individual-income tax rates of 10% to 20% (with 15% most like-

ly), or a rollback of the 1990 and 1993 tax hikes backed by Presidents George Bush and Clinton. The 15% rate cut would reduce taxes by about \$400 for a family with \$40,000 in income; rolling back the earlier tax hikes would have less effect on middle-income workers. Dole aides say that other ideas, such as a credit or deduction for Social Security payroll taxes, are losing ground. Dole will follow up his tax cut with a plan to replace today's tax code with a simplified one- or two-bracket system similar to the "flat tax" backed by many Republicans.

The GOP's goal: Make an issue of slow growth in the Clinton era. While the President can boast of sustained expa-



SURE THING? Voters are questioning how he can cut both taxes and the deficit. "Who is Dole kidding?" a pollster asks

ident a 22-point edge on creating jobs and a 16-point edge on handling the economy.

The public is wary of election-year tax promises, warns independent pollster Gordon S. Black. "Who is Dole kidding?" Black says. "Nobody's going to believe it." Indeed, a June 20-25 NBC News/Wall Street Journal poll of 1,637 registered voters

found 71% dismissed the 15% across-the-board tax cut as "a political gimmick." That's great news for Reform Party contenders Ross Perot and Richard D. Lamm, who deride Dole's growth-by-tax-cuts promises.

Supply-siders still insist such a program will work. Former Housing & Urban Development Secretary Jack Kemp, who sparked the GOP's July 23 tax-cutting conference, says tax reform can double the economy's annual growth to 4.5%. Dole advisers are less ambitious: They figure growth will pay for 30% to 40% of the tax cuts, implying a boost of about 0.4 percentage points in the growth rate.

But academic economists say that Dole's goal is out of reach without a sweeping cleanup of the tax code. They say achieving it might require steps like ending the mortgage-interest deduction, which they say distorts the economy by steering capital into housing rather than business. Such measures are more radical and politically unpalatable than what Dole is considering.

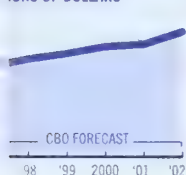
Democrats are already counterattacking. They say Dole's tax cuts would reverse the 60% deficit reduction on Clinton's watch. They're also playing up class warfare: "We don't need new tax breaks for the wealthy paid for out of the hides of working American families," says House Minority Leader Richard A. Gephardt (D-Mo.). With a double-digit lead in the polls, the Clintonites figure they can have fun at Dole's expense. On July 23, the Democratic National Committee set up a toll-free line so Americans could suggest ways to "help Bob Dole formulate an economic plan."

If Ronald Reagan were the candidate, the joke would be on the Democrats. But Bob Dole has never had the Gipper's sales skills—even when he's pitching something he believes in. As a reluctant supply-sider, Dole may have a hard time winning many customers for his tax-cut proposals.

By Mike McNamee and Richard S. Dunham in Washington

BALANCED BY A 'GROWTH AGENDA'

IONS OF DOLLARS



BALANCE THE BUDGET by 2002 with spending cuts.

OVERHAUL THE TAX CODE to create a one- or two-rate system with a postcard tax return.

REDUCE LITIGATION through product-liability and tort reform—particularly important to high-tech companies.

CUT FEDERAL REGULATIONS to reduce business' costs and increase efficiency.

low inflation, and 10 million new real gross domestic product has risen at an average pace of only 2.3% in 1993. Clinton's economists, like most forecasters, see no sharp increase in the rest of the '90s. "This is the best economic recovery since the Great Depression, and it can only be attributed to President Clinton's recording a 1993 tax hike," charges House Majority Leader Richard K. Arney (R-Iowa), a leading flat-tax advocate. Republican strategists hope tax cuts will change the dismal dynamics of the presidential campaign so far. "The second debate shifts to taxes, we start winning," says a senior Dole adviser.

That would be welcome news to Dole's business backers, many of whom are dismayed at his entanglement in issues such as abortion, guns, and tobacco. An economic plan "will energize some key [business] constituencies and show that maybe there's some light at the end of the tunnel," says Karen Kerrigan, president of the Small Business Survival Committee, a lobbying group.

But voters don't seem to share that tax-cut fever. In a Harris Poll of 1,002 adults conducted July 9-13, Americans feel Clinton would do a better job of managing taxes than Dole by a 48% to 41% margin. While the GOP rails against the "Clinton crunch," the poll gives the Pres-

STRATEGIES

AT&T IS BEING BITTEN ON THE ANKLES

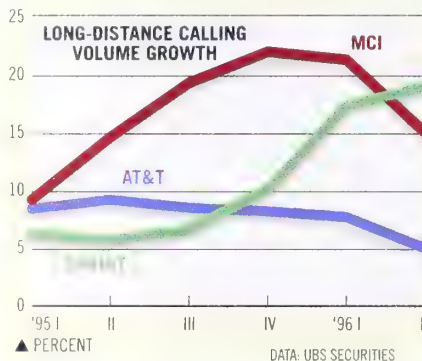
No-name dial-around services steal customers in droves

What's going on at AT&T? On July 18, the nation's largest phone company reported dismal growth in second-quarter call volumes, announcing that the number of minutes carried over its long-distance network for the period increased by only 5%, compared with 15% for MCI Communications Corp. and 19% for Sprint Corp. Bumbled forays into computers, online services, and multimedia ventures are an old story at AT&T, but its core long-distance business was supposed to be a market the company had down cold.

Not any more. The long-distance business is not the oligopoly it was just a year ago, when AT&T, MCI, and Sprint controlled 90% of the \$75 billion in toll calls made in the U.S. The proof: AT&T won as many as 1 million customers from MCI and Sprint in the first half of the year, but volumes still dropped. Plenty new rivals are grabbing customers and blindsiding the telecom giant. And poised on the horizon are the massive Baby Bells, waiting for regulators to allow them into long distance. **MANY SKEPTICS.** AT&T has yet to prove it can thrive in a multifront long-distance market. That's worrisome, given that AT&T Chairman Robert E. Allen's decision last year to break the company into three parts was made precisely so management could focus on telephone ser-

vice. Wall Street was elated with the plan—the company's stock rose as high as 68 after it was announced last September. But now, given the long-distance problems, skeptics abound. AT&T shares are currently trading around 50, below where they were last September before the breakup plan was announced. Some \$28 billion in market capitalization has gone down the drain since February.

GROWTH IS SLOWING AT AT&T



ROBERT ALLEN

Investors are waking up to the fact that AT&T's phone business is coming under siege faster than anyone expected. Most figured AT&T would have two or three years to grab local-calling market share before it needed to worry about losing long-distance share. But now it is clear that that cushion doesn't exist—and the Baby Bells aren't even a problem yet. AT&T lost business over the past three months to a bunch of Lilliputian phone companies such as Telco Commu-

nications, Excel Communications, and American Communications Network. And it barely saw them coming.

These Brand X challengers use a variety of marketing tactics that keep them below AT&T's radar screen. Some provide so-called dial-around service, offering callers the ability to dial an access code that circumvents their long-distance carrier of record. Dial-around rates vary widely, but the services market themselves as a low-cost alternative. They transmit calls over capacity purchased mostly from second-tier carriers Worldcom, Frontier, and LCI International, and all AT&T notices is that its customer is calling less. "Dial-around came up fairly quickly, and we didn't suspect it right away," admits AT&T President Alex J. Mandl.

Prepaid calling cards are another stealth missile. These cards let callers pay in advance for calling time with alternate carriers, and all major carriers have no idea who is buying them. There are multilevel marketers that use independent reps to sell what they often bill as a cheaper, no-name brand of long-distance to friends and relatives for a small commission. Like the dial-around services, some of these alternative carriers are cheaper—though rates are occasionally as much as 40% below AT&T's—but they all market themselves as low-cost alternatives.

ON TARGET. Mandl pledges a fast response to these new competitors. "Our customers apparently believe there's a big price difference," he says. "But their price is often higher. That really is something that we need to explain." Mandl expects that a targeted marketing effort will start showing results this fall. "We will demonstrate to [analysts]

MA BELL'S NEW LONG-DISTANCE RIVALS



DIAL-AROUND COMPANIES

These resellers allow

customers to dial into a discount service on a call-by-call basis, using an access code. AT&T can spend millions to retain customers and still lose their business.



PREPAID CALLING CARDS

Like the dial-around com-

panies, prepaid calling cards give customers a way to circumvent their long-distance carrier of record, again without giving AT&T any notification.



LOCAL PHONE COMPANIES

Within three years, local

phone companies will be allowed to offer long-distance calling within their regions for the first time; they can already do so outside their home markets.



INTERNET CALLING

Only about 500,000 people worldwide

use the Internet for some voice communication today. If glitches in the technology can be worked out, the Internet will provide flat-rate long-distance and international calling.

at have changed their view that we n and will grow this business," he ys.

But AT&T watchers are clearly worried that the company has fundamental problems. To begin with, it is more dependent on the consumer market than Sprint. In the past, AT&T could least count on the loyalty of its customers, the ones least likely to switch carriers. No longer. "We are seeing more people for the first time leaving AT&T," says LCI Chairman H. Brian Thompson, whose long-distance telecommunications company uses multilevel marketers. "More of our customers come

from AT&T than from any other source."

There are also nascent challenges looming. The Baby Bells are the most notable. But down the road, long-distance phone calls over the Internet, which would only cost as much as the initial connection, could affect the pricing structure of long-distance calling, mandating a flat rate rather than per-minute charges. Mandl says that's one reason AT&T is getting into Internet access—to grab those callers' business.

No one is counting AT&T out just yet. "AT&T has been a very aggressive competitor in the last four to six years," says Gary D. Forsee, head of Sprint's

long-distance business. The company is also entering an era where carriers will sell bundles of services, with long distance just one part. AT&T is better placed than any other carrier to compete in such a market, what with its huge cellular network, its plans to offer local calling in every state, its stake in a pay-TV service, and its aggressive Internet scheme. But AT&T has yet to offer a multiservice package—even though it can ill afford to lose more customers. Without some new offering, dial-around services could be the least of its worries.

By Catherine Arnst in New York, with Amy Barrett in Washington

CALLING ALL NET SURFERS

It's not just for chat rooms. On the Internet, using your PC and the right software, you can call almost anywhere and talk as long as you like for no more than your Internet access fee—around \$20 a month in the U.S. The audio quality isn't great, and you can speak only with other PC users running the same software. Yet there's

probably some form of Internet phoning in your future, especially now that the two biggest players in the PC industry have thrown their muscle behind the concept. On July 17, Intel Corp. and Microsoft Corp. announced their backing of a set of key technical standards that may cause the nascent Internet telephony market to take off—eventually. **"LEADERSHIP."** Until now, the software for Net phoning has been supplied mainly by

startup companies with names such as VocalTec, NetSpeak, and VoxWare. But an absence of uniform technical standards left their products mutually incompatible. As a result, regular weekly usage of Net phoning has been limited to only about 30,000 hobbyists, estimates Jeffrey L. Pulver, president of Pulver.com Inc., a consulting firm. "Intel and Microsoft backing a standard will greatly expand the market," Pulver says. "This is the first time we've had leadership in the industry."

Making the Intel-Microsoft standards likely to catch on is Microsoft's plan to build them into Windows 95. Once that happens, Pulver says, software makers will find it easy to build all sorts of Internet telephony products. Companies such as 3DO, Virgin Interactive, and Sierra On-Line have demonstrated computer games that

a Web-based call-distribution system to help catalog companies do business over the Web—in lieu of 1-800 lines. Besides routing incoming Net calls to operators, it will let them send Web pages back to customers while they talk.

GATEWAYS. The Intel-Microsoft alliance "shows that [Net telephoning] is not just for hobbyists," says Elon

A. Ganor, president of VocalTec Inc., whose \$49 Internet Phone software is currently the market leader.

VocalTec, its many small rivals, and telephone-equipment companies such as Lucent Technologies, Ericsson, and Northern Telecom figure corporate buyers represent their largest market for Net-phoning products. They're scrambling to build hardware-based gateways that will allow people to dial and speak

over a standard phone but have their calls transported over the Internet's low-cost links. As much as 16% of U.S. voice-traffic volume could be moving over the Internet by 2000, says Hilary Mine, an analyst at Probe Research.

Most of this traffic, she notes, will not replace traditional phoning. It will exist solely because Internet calling will be so inexpensive relative to standard phone rates. Make it cheaper, and people will buy more.

By John W. Verity in New York



Until now, Net phoning has been limited to a small group of hobbyists—but Intel and Microsoft could change all that

let players verbally taunt each other—or collaborate against other teams—across the Net. Microsoft and others are developing programs that let groups of people concurrently view, edit, and discuss PC documents across virtually any distance.

Together, the companies active in Net phoning are "creating a whole new telephone system," with even more functionality than standard phone equipment, says Robert Kennedy, president of NetSpeak Corp. NetSpeak itself is working on

COMMENTARY

By John A. Byrne and Gail DeGeorge

DEAR AL: PUT AWAY THE CHAINSAW

Memo to: Albert J. Dunlap, a.k.a. "Chainsaw Al"
Chief Executive
Sunbeam Corp.

Dear Al:

So you finally landed a job as chairman and chief executive of yet another company. And already, Wall Street is applauding. The day after your July 18 appointment as head of Sunbeam Corp., the troubled appliance maker's stock surged nearly 50%, to \$18.625 a share. Even before you showed up for work, Al, you made Sunbeam's disgruntled shareholders more than half a billion bucks.

You know why Wall Street has irrationally bid up the stock. Everyone expects you to do what you always do: cut jobs, divest assets, and then ditch the company at a tidy profit, just as you did at Scott Paper Co. That's why many think of you not as a turnaround artist but as some kind of corporate vivisectionist.

Well, Al, here's the chance to prove them wrong. Sunbeam is your opportunity to show the critics that you can manage a company over the long haul. Even though it's much smaller than the big companies you've criticized—including Westinghouse Electric, Eastman Kodak, and IBM—Sunbeam, with its \$1.2 billion in annual revenues, will be an honorable testing ground for your management skills.

NOT BLOATED. This one won't be easy. In Sunbeam, you're not going to find a company that is about to ride the crest of an industry cycle, as you did at Scott. You also won't discover an opulent and bloated corporate headquarters populated by 1,600 employees. Sunbeam has just 60 staffers at its Fort Lauderdale (Fla.) headquarters. Also unlike Scott, Sunbeam isn't spending \$30 million a year on consultants. Still, the company's earnings have fallen below expectations in five of the past six quarters, and second-quarter earnings are down 36%.

Al, here are a few things you ought to do if you want to run this for a while:

- Check your ego at the door. You no longer need a high-priced public-relations executive from Burson-Marsteller to hawk every move you make and, hopefully, push up the stock price—especially if your intention is to revitalize and manage Sunbeam for the long haul.

- Leave your hatchet, or chainsaw, in your garage in Boca Raton, Fla. Sure, it's your trademark. And already, you've been initiating some major changes, such as replacing North American President and Chief Operating Officer James Clegg with Russell A.

Kersh, a long-time pal who worked with you for years, and publicly mulling a major reorganization. But Sunbeam has already been through a slash-and-burn exercise before. Changes there should be made with a scalpel, not a chainsaw.

- Invest in new product development. The company's well-known Sunbeam and Oster brands are a valuable franchise. But there's a sore need for new products to take advantage of that brand equity. At Sunbeam, you won't be able to just put a blender or gas grill in new packaging—the kind of thing you often did at Scott—and hope that it sells.

- Improve relationships with top retailers. Sunbeam has lost shelf space in key stores in recent years, and its market share has slipped in such core categories as blenders, mixers, can openers, and outdoor grills. You'll need to offer the major retailers some powerful incentives to win



DUNLAP'S WAY

Everyone expects you to cut jobs, divest assets, then ditch the company at a tidy profit, but Sunbeam is your chance to prove you can manage a company over the long haul

them back. And you won't be able to pass on double-digit price increases to consumers as you did at Scott.

- Boost manufacturing efficiency. Sunbeam has yet to take full advantage of a new, \$80 million facility for houseware products in Hattiesburg, Miss., which still isn't operating at full capacity. To do that, you will need to consolidate manufacturing from the 40 factories and distribution centers that Sunbeam already owns or leases. Perhaps you can simply accelerate the plans on the drawing board to close down three or four plants.

It's a tall order, Al. Especially when you're already in the money—even before you showed up for work. The 2.5 million stock options Sunbeam gave

you to come aboard are already worth \$30 million. The 1 million shares of restricted stock you were given are worth another \$18 million. And, of course, you have that \$1 million annual salary. Heck, Al, you made \$48 million before you fired anyone or barked a single order as the new chief executive.

That means it's going to be real tempting to do what Wall Street wants and expects: just clean it up enough to get rid of it. But don't do it, Al. Give it a shot. Show us you have what it takes to really turn around a business.

Byrne writes about management. DeGeorge covers Sunbeam from Miami.

HEAVY EQUIPMENT GETS INTO GEAR

Quarterly management helps profits climb despite modest sales

h, revenge is sweet. For years, equipment manufacturers were stuck in the shadows while such high-flyer sectors as technology basked in the spotlight. Makers of tractors, combines, and other heavy equipment had modest growth prospects, dangerous business cycles, and nagging overcapacity. But in the second quarter, as tech companies stumbled, heavy manufacturers surprised Wall Street with unexpectedly strong profits. Caterpillar Inc. reported quarterly earnings 16% above the same quarter last year, well above

Canada, and European countries start to recover. For instance, Deere & Co.'s exports in the six months that ended April 30 were up 12%, to \$723 million. And Deere will benefit from a \$187 million combine contract for the Ukraine when it reports fiscal third-quarter results in August.

That doesn't mean that double-digit growth is returning to heavy industry. Unit sales of construction equipment are expected to increase only 3% to 4% annually in coming years and ag equipment sales are in a long-term slide.

to unload product at discounted prices. Now, says Robert W. Lane, senior vice-president and chief financial officer at Deere, "We're positioning ourselves to be more disciplined on the downside." Deere and other big manufacturers also are pushing their dealers to keep no more than four months of inventory on hand. And the companies are keeping their own stocks way down, as well. In 1988, for instance, Deere's inventories rose to 17% of goods sold as sales surged. But no more. During 1995, even as revenues soared 14%, inventories stayed at 10% of goods sold.

BRUISING. Labor costs also have been slashed. Deere's workforce of 33,000 is half what it was in 1980. Case is in the midst of a four-year restructuring. And Caterpillar gave its CEO, Donald V. Fites, a 75% pay increase in 1995, to \$3.1 million, for aggressive cost-cutting that included winning a bruising battle with the United Auto Workers. Overall, op-

HARVESTING PROFITS

Why manufacturers of heavy equipment are pulling in the green

REDUCED COSTS Major cost-cutting programs at Caterpillar, Case, Deere, and others have improved operating margins to about 13%, on average, from about 7% five years ago.

TIGHT CONTROLS Average inventories are now down to about four months of sales, about half the historical average. That has helped keep prices firm.

analysts' expectations. Case Corp. announced a 21% surge in operating earnings. And net income at Ingersoll-Rand Co. rose 39%, again handily beating forecasts. With investors' ravenous demand for cyclical stocks in a rising market, the share prices the group haven't done especially well—but they've outperformed the techies. From July 1 through July 23, Standard & Poor's index of diversified machinery makers was off 8.7%, vs. 7.8% for the S. 500. But the tech-heavy NASDAQ composite index fell a whopping 14.1%.

RISK EXPORTS. Wall Street jitters about strong earnings among the big manufacturers are another sign of the S. economy's strength. Cat, which previously expected 1996 sales to decline because of sluggish 1% economic growth, now figures that a 2% to 2.5% expansion will help this year's sales reach or exceed 1995 figures. Exports are brisk—and may get a further boost now as the economies of Mexico,



UKRAINE-BOUND COMBINES: Deere and other companies are benefiting from improving economies abroad

What's changed is that the manufacturers are doing far better than before at keeping costs under control. Now, with the economy purring along better than expected, profits are soaring. "Rigidity has been common in heavy industry," says Jean-Pierre Rosso, Case's chairman and chief executive. "Now we're finding that we can run the business with fewer assets, lower costs, and a lot more flexibility."

Inventory management has been particularly critical. During boom times, dealers used to stock up until they could cover sales for eight to ten months. When demand sagged, they were forced

REDUCED COMPETITION

After the vicious cycles of the past, only three or four major competitors remain in most product categories. In farm equipment, only five major players remain, compared with 20 companies 12 years ago.

STRONG DOLLAR Favorable currency transactions are giving profits a boost.

DATA: BUSINESS WEEK

erating margins at equipment makers are expected to jump to about 13% this year, up from 7% five years ago. It doesn't hurt that there is far less competition than there once was. In agricultural equipment, for example, there are just five big players now, including Deere, Case, and Japan's Kubota.

Heavy-equipment makers aren't pretending the hard times are all behind them. One big worry is that the strengthening dollar will cut into export growth, offsetting the positive effects of economic recoveries abroad. Wall Street also worries an economic downturn will hit big manufacturers hard. Indeed, surveys show that the rate of growth in spending on low-tech capital equipment is slowing this year. "This industry has not lost its cyclicality," says Deere's Lane. That's for sure. But as recent earnings reports show, the companies are much better managed now—in good times and bad.

By Peter Elstrom in Chicago

CRISIS MANAGEMENT

HOW TWA FACED THE NIGHTMARE

Bad luck at several stages hampered the airline's response

It was 2 a.m. London time when Jeffrey H. Erickson, the gruff, low-key engineer who heads Trans World Airlines Inc., got the call every airline executive dreads. Joseph Vilmain, TWA's international vice-president, woke Erickson at a hotel in London, where the CEO had traveled on business. His horrible news: TWA Flight 800 from New York to Paris had crashed off the coast of Long Island. "I can't describe what it was like," says Erickson, who found himself shaking after he hung up.

The ultimate lessons of the TWA crash can't be known until the cause is determined and analyzed. But the tale of TWA's response to the catastrophe, culled from Erickson, other insiders, and outside experts, shows that the carrier, hindered by considerable bad luck and lean management, actually did fairly well in managing the crisis—despite widespread criticism.

The first bit of ill-chance was that Erickson was in London rather than three hours away at the carrier's St. Louis base. The CEO and Mark Abels, a public-relations executive with him in London, scrambled to charter a private plane to fly them to New York. Even so, it was 10 a.m. on July 18, some 13 hours after the crash, before they arrived at TWA's hangar at John F. Kennedy International Airport.

SHORT-STAFFED. By that time, Erickson and Abels knew from updates during the flight from London that it was unlikely anyone on Flight 800 had survived. Erickson, 51, is a veteran airline executive. But none of the carriers he had worked for, which include Reno Air Inc. and Aloha Airgroup Inc., had suffered a major crash on his watch. And by the time he arrived in New York, politicians such as New York Mayor Rudolph W. Giuliani had been on the

scene for hours—and were loudly criticizing TWA's slow response.

The problem wasn't just Erickson's delayed arrival. There was also a dearth of other top managers who were available to respond. Two who could have filled the void while Erickson was traveling—Mark J. Coleman, the company's marketing senior vice-president, and CFO Robert A. Peiser—had resigned just a month earlier over a strategy dispute with Erickson. In fact, many TWA managers in St.



TAKING THE HEAT
CEO Erickson praises TWA's crisis team in general but says that notification of passengers' families "should have gone faster"

Louis were attending a going-away party for Coleman when a chorus of beepers went off, cutting short the celebration. With management so sparse, Senior Vice-President of Operations Don Monteath had to man the crisis center in St. Louis, leaving a void in New York until Erickson arrived.

Another difficulty: As a smaller airline, TWA has only one "trauma team" of 650 employee volunteers scattered across the country; larger carriers have regional response teams. Johanna O'Flaherty, the human resources executive who heads the team, was vacationing in Santa Barbara, Calif., when she heard the

news. American Airlines delayed its last red-eye out of Los Angeles so she could get to New York Thursday morning. But getting the whole team to New York ate up precious hours. Dozens were there by noon on Thursday, July 18, and 100 by that evening. They took over the Ramada Plaza hotel as a central command center at the Hilton Hotel near JFK.

AVOIDING ERRORS. Too slow? The National Transportation Safety Board allowed the airline to begin notifying families about 9 a.m. Thursday morning. That evening, all families had been contacted. That's considered reasonably fast by industry standards: It took United Airlines four days to issue a list of passengers who it believed to be dead after July 19, 1989, crash in Sioux City, Iowa.

Erickson says he thinks TWA's notification "should have gone faster." He praises his team's efforts, especially considering that 60 families had to be tracked down in France. TWA also avoided horrible mistakes by being careful.

Some passengers on Flight 800's manifest actually missed the flight, including several who were delayed in Chicago by heavy rain.

Once the immediate crisis is dealt with, TWA will have to focus again in building its franchise. Erickson, who grew

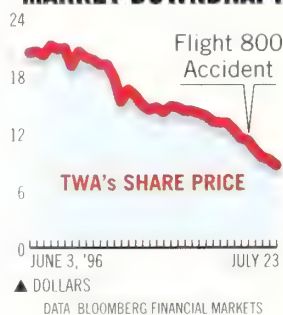
up in Suffolk County near the crash site, saved TWA two years ago by delaying recruiting a new management team, persuading creditors to accept a \$100 million write-down of debt, and guiding the company through a prepackaged bankruptcy last August. But if the crash taints TWA's reputation badly, its financial recovery—even its survival—could be in question. PanAm Corp., for instance,

never recovered after the December, 1988, terrorist bombing of Flight 103 over Lockerbie, Scotland.

Much will depend on the cause of the crash, experts say. But regardless of that, TWA will survive, Erickson pledges: "PanAm was a distressed carrier. We are not."

By Susan Chandler in Chicago

MARKET DOWNDRAFT



THE MAN BEHIND BRAND SHAQ

Agent Leonard Armato speaks softly but drives a hard deal

At 2 a.m. on July 18, the Shaq Inc. brain trust was settling into a ninth-floor suite in Atlanta's West Peachtree Plaza. Unofficial chairman of this two-man marketing powerhouse, basketball superstar Shaquille O'Neal, was making his way up from the Olympic Village. Working the phones between Orlando and Los Angeles, Leonard Armato, O'Neal's agent, was doing what he does best: stoking the earning potential of the most famous 7-footer in America.

By 2:30 a.m., the 24-year-old O'Neal was undoubtedly among the wealthiest as well. A six-day bidding war between the Orlando Magic and Los Angeles Lakers had won O'Neal a seven-year deal with the Lakers worth an estimated \$120 million. For Armato, a low-key, Brooklyn-born lawyer, it's just the latest piece of a marketing blitz designed to make his backboard-smashing client the most ubiquitous brand name in sports. From the moment O'Neal joined the National Basketball Assn. as its top draft choice in 1992, Armato has promoted the quiet giant like a shiny new toy model. In all, Shaq will earn a staggering \$20 million this year by pumping products for the likes of PepsiCo, Reebok International, Neilson Cadbury, and Spalding. But Shaq Inc. is far more than a typical sports promo machine. Indeed, you can watch the 300-pounder on his hip label, interactive game, Web site, or in his two movies. "It's multimedia marketing of a brand that happens to be Shaquille O'Neal," says Armato. "Walt Disney started with a mouse and created an entertainment empire. We're starting with one of the world's great basketball players."

ROUND RULES. Armato drives tough deals. Even before O'Neal played his first pro game, the agent won him a lucrative Reebok International Ltd. contract by pitting Reebok against rival Nike Inc. And to be a part of team Shaq, companies have to play by

Armato's rules. That means using the O'Neal-trademarked logo on Shaq products, paying Shaq a royalty, and cross-promoting him. In concert with Disney's July 17 release of *Kazaam*, in which O'Neal plays a genie, Neilson Cadbury put a picture of him in costume on a Mr.

LEONARD ARMATO

CEO, Management Plus Enterprises

AGE 43 HEIGHT 6' 0"

CLIENTS Shaquille O'Neal, Hakeem Olajuwon, Ronnie Lott

EDUCATION BA, 1975, University of the Pacific, where he was an all-league basketball player; JD, University of San Diego Law School, 1978

CAREER PATH Started as a lawyer with Sullivan, Jones & Archer, San Diego; switched to Los Angeles, 1981; sets up agency in 1990; also served from 1983 to 1988 as executive director of the Association of Volleyball Professionals

PERSONAL Divorced, two kids. Dating Olympic volleyball player Holly McPeak.

FROM BROOKLYN TO BABYLON: Big plans for L.A.

Big candy bar, PepsiCo's Taco Bell unit offered *Kazaam* products with kids meals, and Reebok launched a *Kazaam* sneaker line. Such deals have made Armato a star sports agent, even though he only represents a handful of clients. O'Neal alone keeps him busy. On top of collecting his fee for negotiating deals, he is executive producer of *Kazaam* and runs Shaq's TWISM record label.

GOOD TIMING. Armato, a onetime guard who averaged 12.8 points a game on the University of the Pacific hoop team, got his start working with sports companies as an outside lawyer for apparel maker Fila Sport and sneaker company L. A. Gear Inc. in the mid-'80s. He helped guide Laker great Kareem Abdul-Jabbar out of near-bankruptcy in 1987, partially by signing him to a sneaker deal with L. A. Gear. Armato also showed a knack for timing: He signed O'Neal's college coach, Louisiana State University's Dale Brown, to an L. A. Gear contract shortly before Brown introduced him to Shaq.

Armato's negotiating tactics are hard-edged. A few years back, he had client Brian Shaw jilt the Boston Celtics and play a season in Italy, only to return to the Celtics the following year for a hefty salary hike. But some of Armato's deals haven't panned out as well for the companies involved. A "Shaq Attack" clothing line that Armato pressured Reebok to launch, for instance, hasn't sold particularly well, says Reebok Executive Vice-President Tom Carmody.

Still, O'Neal does sell sneakers. So Carmody will be among the executives who trek to Los Angeles in September when Armato convenes his annual "Shaq summit" of O'Neal marketing partners. Armato is already preparing Shaq's next film, a joint venture with producer Quincy Jones based

on the DC Comics character Steel. A rap clothing line is also coming. "When you take a star of Shaq's magnitude and bring him to Los Angeles, the possibilities are endless," says Magic Johnson's agent, Lon Rosen.

What next? A Shaq TV show? Or Saturday morning cartoon? Armato isn't saying. But once Shaq hits the world's entertainment capital, expect the slam-dunk deals to proliferate.

By Ronald Grover in Los Angeles



COMMENTARY

By Eric Schine

SAVE CALIFORNIA'S REDWOODS—BUT NOT THIS WAY

Consider it the Charles E. Hurwitz Relief Fund. After bailing out the Texas dealmaker's failed savings and loan association to the tune of \$1.6 billion, the U.S. government is now on the verge of doling out thousands of acres and hundreds of millions of dollars' worth of federal lands to him. The package of properties would include valuable timberlands and may contain such gems as the aptly named Treasure Island, a rare parcel of undeveloped San Francisco Bay real estate recently vacated by the Navy.

Why would the Clinton Administration cut such a deal? Hurwitz, chief executive of Houston-based Maxxam Inc., is currently the target of a Federal Deposit Insurance Corp. lawsuit and an Office of Thrift Supervision complaint alleging mismanagement of the United Savings Assn. thrift, which went under in 1988. He faces potential liabilities in the two actions of nearly \$750 million. But Hurwitz, a central figure in the Drexel Burnham Lambert Inc. junk-bond deals of the 1980s, also controls Pacific Lumber Co. and its rare 3,000-acre stand of old-growth redwoods, Headwaters Forest. Hurwitz declined to comment, but he has said in the past that the government actions are "without merit" and asserted that the S&L failure resulted from the collapse of the Texas economy.

GREEN POINTS. Hurwitz has been trying to chop down Headwaters Forest for nearly a decade. But blocked by activists and court actions, he hasn't been able to get at it. He claims the lumber is worth at least \$700 million, and he has even filed "takings" suits against the U.S. and the state of California, charging that they have denied his company use of its property. "We expect just compensation," says Pacific Lumber President John A. Campbell. The

suits are pending. So Hurwitz now is proposing to swap the forest for federal lands of equal value. And, eager to score green points in an election year, the Administration seems all too eager to take the bait.

It shouldn't. Saving the redwoods and the wildlife they harbor is a critical goal. But the Administration has another option, and so does Hurwitz. If the government dropped the thrift-related charges against Hur-

ing Hurwitz prime federal acreage, negotiators could easily wind up giving away too much. Development rights to Treasure Island alone could be worth several hundred million dollars. It doesn't help that handling the talks for Clinton is Deputy Interior Secretary John R. Garamendi, the former California Insurance Commissioner, who may be overly eager to get a deal done. "The door is open for serious negotiations," he

says. Hurwitz, on the other hand, is legendary for his brilliant, brinkmanship bargaining tactics.

"ATTILA." Some officials realize what they're up against. Says one close to the talks: "It's a game for Hurwitz. He's rich, powerful, and knows he has the one thing we want." Some insist they have little choice. "If Attila the Hun has the Mona Lisa and you want it back, you deal with Attila the Hun," says Representative George Miller (D-Calif.).

But that is exactly the same flawed logic that the townsfolk adopted in Scotia, Calif., when Hurwitz acquired Pacific Lumber in 1986. For decades, Pacific Lumber thrived as a conservatively managed

steward of its forest holdings, cutting down just what it needed to turn a tidy profit and keep the locals employed. Hurwitz promised he would maintain the tradition. But once he bought the company, he doubled production rates to clear-cut thousands of acres of old-growth redwoods.

Headwaters Forest should be saved. For now, Hurwitz isn't interested in anything but a land deal. But the Administration shouldn't be in any rush to hand over federal land. If it proceeds with its scheme to buy off Hurwitz, we can all chalk it up to greenmail, in the greenest sense of the word.

Schine covers California politics.



Activists have foiled Hurwitz' timber plans for a decade. Fed up, he wants to swap his forest for federal lands

witz in exchange for taking title on the Headwaters Forest, it would limit its costs in the deal. For his part, Hurwitz could rid Maxxam of a cloud that has been a factor depressing its share price for years. He could also achieve a major public-relations coup.

Such a trade may sound outlandish, but the government has resorted to similar solutions before. Starting in the 1980s, for instance, the U.S. federal government released several Latin American countries from debt obligations in exchange for the creation of protected parklands and the like in their countries.

In addition to smacking of election-year politics, the land-for-land proposal creates the risk that by giv-

IN UPDRAFT FOR CORPORATE JETS

Planes are so hot that even used ones are in short supply

When Jack Welch gets an idea, he works it. During a call a few months ago with Boeing Co. CEO Phil Condit, the General Electric Co. CEO mused about his desire for something bigger than the Gulfstream Aerospace Corp. G-IVS GE now uses. What about the GE-powered Boeing 737, Welch asked? Condit agreed the plane could be modified for executive use. Presto. On July 1, GE and Boeing launched Boeing Business Jets, a joint venture. GE will get the first two of these \$35 million jets, able to fly nonstop from New York to Tokyo. "We think this is a new era of global transportation for the business traveler," says Welch.

FLYING FAXES. At as much as \$3,500 an hour in operating costs, such jets are still only for the rich. Still, demand for corporate planes is on the rise. Business jet sales soared 23% last year, to \$2.06

billion, and sales are expected to climb 10% more in 1996. At Gulfstream, the order backlog for its \$35 million G-V is near \$3 billion. Industry sources say buyers include: IBM, Gannett, Time Warner, and Seagram. "You can't even find a used G-IV in the market right now," says Al Lane, manager of flight services for

HIGH OFFICE

Layouts might include conference rooms and even a fitness area

Amoco Corp.

Part of what will drive future increases: the introduction of several new long-range models during the next 18 months. Boeing will deliver some 10 jets annually, beginning in 1998. Bombardier Inc., meanwhile, is spending \$800 million to develop the Global Express, which can carry 12 passengers nonstop from Toronto to Beijing.

Executives say they need the jets to be globally competitive. "If you go out and make one deal, it makes sense" to

invest in a plane, says David Linenmeier, director of aviation for H. Wayne Huizenga's Huizenga Holdings.

Options on the new planes go well beyond office furniture. Boeing says interior layouts might include conference rooms, offices, a bath and shower, and a fitness area. The space could even be reconfigured between flights. Other popular options: state-of-the-art sound systems and the latest global navigation and weather gear. Ex-



Executives "want phones with triple lines so you can talk and fax, as well as get accurate weather information," says Bryan Moss, vice-chairman of Gulfstream.

Those requests mark a change from the 1970s, when company planes were full of deep-pile carpeting and gold-plated faucets. Gold may be out, but the 1990s models still beat flying commercial.

By Tim Smart in New Haven, with Seanna Browder in Seattle

IE OLYMPICS

ET THE '04 GAMES BEGIN

The bidding is already in high gear to play host after Sydney

Augustin C. Arroyo is not a celebrity. But he's being treated like one during Atlanta's Centennial Olympic Games. The chubby, mustachioed Arroyo, an Ecuadorian member of the International Olympic Committee, will meet with sports ministers from close to a dozen countries, view Turkish art treasures at an exclusive party, and wind at an Italian fashion show. The reason: Arroyo is a member of the 112-person team that anoints host cities for future Olympic Games. And, as he says, "you want to kiss, you have search for the mouth."

Let the puckering begin. Some 11 cities are vying to bring home the 2004 Summer Games after Sydney hosts them in 2000. The Atlanta games mark the start of a mating dance that will conclude in Sep-

tember, 1997, when IOC President Juan Antonio Samaranch is to announce who will snag the rings.

It's a high-stakes contest. Atlanta expects to see a \$5.1 billion economic impact from the games, including a new stadium and new roads. But profits aren't a certainty. The 1976 Olympic circus left Montreal with a \$1 billion debt, after labor strife and rampant corruption at the top levels of its Olympic hierarchy quadrupled the games' cost.

Still, each bid city is convinced it can handle the event, and they're pulling out all the stops to get it. Take Cape Town, South Africa. On July 21, Archbishop Desmond Tutu threw his weight behind Cape Town's bid while hosting a

church service in downtown Atlanta. "The archbishop helps us to create awareness and a high level of credibility," explains Chris Ball, chief executive of the Cape Town bid.

Other cities are banking on costly campaigns to catch the attention of IOC members. Stockholm has shelled out nearly \$1 million on a lavish hospitality suite and a pavilion. Rome is throwing a fashion show. Turkey, which is trying to lure the Olympics to Istanbul, hosted an elite party July 22 at Turkey House. Samaranch made a brief appearance as other IOC members nibbled Turkish pita bread and rubbed elbows with sports celebrities.

BRINGING IT BACK HOME. Athens, though, is taking a more low-key approach. Having lost a bid to host the Centennial Olympics, it is quietly touting its infrastructure and facilities, barely mentioning its role as the birthplace of the games.

The consensus among some bid cities is that the IOC favorites are Rome, Stockholm, and Athens. But IOC Marketing Director Michael R. Payne warns: "It's difficult to tell until we've looked at all the facts and figures." Meanwhile, the bid cities will compete in an Olympic event of their own.

By Nicole Harris in Atlanta



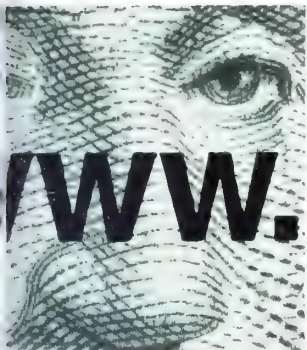
LONG-DISTANCE LOBBYING: At Atlanta's Turkish House

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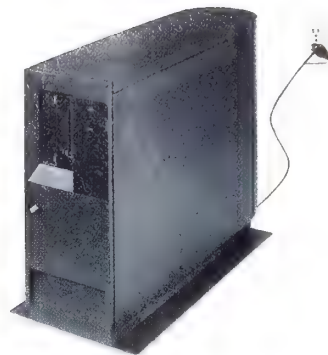
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In Business This Week

EDITED BY KELLEY HOLLAND

ENRON'S UTILITY PLAY

AS THE SAFE, PROTECTED world of gas marketers collapsed in the mid-1980s, Kenneth Lay merged four pipeline companies to create Enron, the nation's leading natural gas supplier. Now Lay, a former U.S. deputy under secretary for energy, will pioneer the deregulation of electric utilities. On July 22, Enron's CEO laid out plans to buy Portland General for \$3.2 billion in stock and assured debt in what would be the first merger of a utility and a gas supplier. Lay says he realizes rivals are not going to stand still in this brave new world. But, he says, "we're positioned better than any other company to become the largest,

most profitable company in North American energy markets. That's our goal."

DOES A BARNEYS DEAL FIT?

BARNEYS NEW YORK, FOR seven decades painstakingly private, is becoming more public by the day. Six months after filing for bankruptcy, the upscale apparel chain's secret talks with suitors have burst into public. On July 23, Saks Holdings announced that it would join with Barneys' disgruntled Japanese partner, Isetan, to devise a reorganization plan. Barneys blasted the agreement. One problem for Barneys: Such a deal would throw into question the fate of Bob and Gene Pressman, the brothers who are co-chief executives.

CALDERA FILES A MICROSOFT SUIT

SEEMS LIKE OLD TIMES. Caldera, a company owned mainly by Ray Noorda, Microsoft CEO Bill Gates' old nemesis from Novell, has filed an antitrust suit against Microsoft. Caldera has acquired DR-DOS, an old operating system that once competed against MS-DOS, from Novell. DR-DOS reached just \$30 million in sales at Novell, and hasn't been viewed as a serious rival of MS-DOS for more than a decade. Nonetheless, Noorda, who helped start the antitrust fight against Microsoft that culminated in a consent decree in 1994, is taking up the cause again. This time, a Caldera attorney says, the company hopes to finish the job "the Justice Department left unfinished."

A PAY CUT FOR GM'S NEW HIRES

SOME GENERAL MOTORS workers are agreeing to wage

HEADLINER: JAMES NEAR

HE ALWAYS FOUND THE BEEF

Were it not for James Near, Dave Thomas, founder and senior chairman of Wendy's, might never have become an ad icon. Near, as president of Wendy's in the late 1980s, persuaded Thomas to become one of the restaurant industry's most popular pitchmen.

The legacy, though, of the man who rose from short-order cook at Burger Boy to chairman of Wendy's at his death from a heart attack on July 22, at age 58, will be of a canny strategist who cared deeply for his customers.

After hanging up his apron at Burger Boy, Near

became a franchisee in 1974. He later started Sisters Chicken & Biscuits and sold it to Wendy's in 1980. In 1986, he was asked to fix the ailing burger chain. Thomas took a back seat, and even had cards printed saying "Jim's Right Hand Man."

Near became CEO in 1989 and chairman in 1991, and he handed over the CEO job to Gordon Teter in 1995.

Wendy's has not yet named a new chairman. The challenge is to find one who answers the question "Where's the beef?" as well as Near.

By Rick Melche



CLOSING BELL

NAVIGATE THIS

Investors' cooling ardor for Internet stocks is hurting Netscape, the granddaddy of cyberspace startups. The company, which makes Internet browsers and Web site software, will face growing pressure in the next six months as Microsoft delivers its own improved Web packages. Although Netscape on July 18 reported record revenues and earnings for its second quarter, investors spooked by Microsoft drove Netscape shares down 25%, from 56% to 42%, from July 18 to July 23.



cuts for new hires in the interest of protecting their own jobs. Unionized electrical workers at GM's parts plant in Moraine, Ohio, agreed July 22 to a 15-year pact that allows GM to pay new hires about half of the \$19 hourly wages of current workers. In exchange, GM will keep the plant open until 2011. That deal will be hard to sell to the United Auto Workers. But it shows the high price GM will demand if UAW President Stephen Yokich really wants to preserve union jobs in contract talks this fall. The current contract expires on Sept. 14.

ABC MAKES COLLEGE BOWL YARDAGE

WHO IS NO. 1 IN COLLEGE football? ABC will spend about \$500 million to help settle the question. Starting in 1998, the college bowl games will be rejiggered so that the top two

teams will always face off at the end of the season. Currently, some divisions are committed to certain bowls, so the two top college teams often don't play each other. ABC now will broadcast a total of four bowl games in a seven-year deal. The loser in this: CBS Sports, which has rights to the Fiesta and Orange bowls through 2001. The CBS agreement had an opt-out clause that lets the Fiesta and Orange bowls sign with ABC if they choose to.

ET CETERA...

- ValuJet's flight attendant union wants to oust its chairman and president.
- MasterCard and GTE may launch a new secure Internet commerce system.
- Cereal maker Ralcorp sold its ski resort subsidiary Vail Resorts for \$310 million.
- Morrison Knudsen and shareholders have developed a new reorganization plan.

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Chances are you won't be seeing it anyway. Because *The Daily Olympian* is for the athletes — relating vital news about training schedules, ceremonies and social events. It's part of the incredible flow of information that will be generated in Atlanta, some of it electronically, much of it on paper. Much of it on *our* paper, in fact. There's one little irony about the digital age. Paper — including new, higher performance varieties — is as essential as ever.



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EDITED BY OWEN ULLMANN

AN END TO WELFARE POLITICS AS WE KNOW IT?

For four years, Democrats and Republicans have devoted more energy to playing politics with welfare reform than trying to overhaul a system in need of repair. President Clinton waited two years just to introduce his plan, and Capitol Hill Republicans sent him two draconian versions designed to prompt vetoes. Now Congress is at it again—and the third try may be the charm.

This time, politics might be the driving force behind passage. With Election Day nearing, Clinton fervently wants to fulfill his 1992 pledge to “end welfare as we know it” by signing a reform bill. And many Hill Republicans, worried about their own reelection, want to bring something home to voters and shed the “extremist” label pinned on them by Democrats. So they’re willing to accept less-stringent reform and share credit with Clinton.

TOUGHER BILL. That’s why the Senate voted 74-24 on July 23 for a moderate plan. It would end the unlimited 60-year-old federal welfare entitlement to mothers and children by cutting aid to adults who don’t accept work or training after 10 years, and capping lifetime benefits at five years. A House-Senate conference will work out differences with a tougher version approved earlier by the House. The outlook: a final agreement, possibly by August, that Clinton will sign. The President says the latest measure is still too tough on poor children, but senior White House aides praise it as a serious attempt at compromise and not just veto bait. “I’m optimistic we can make it even better in the conference,” Clinton predicted.

The President isn’t alone in looking for a way out on welfare. Senate Majority Leader Trent Lott (R-Miss.)—who replaced GOP Presidential candidate Bob Dole in June—wants to demonstrate his clout and counter charges that the Republican Congress is gridlocked. “The best politics is to do what’s

right for the country...not on the basis of party,” Lott says.

Still, daunting obstacles remain. The chief political snag is Dole’s flagging campaign. The Kansan has been counting on using Clinton’s vetoes as a potent issue this fall. So Dole’s advisers are loath to see Clinton get off the hook and, worse, take credit for welfare reform. Dole has an ally in House Speaker Newt Gingrich (R-Ga.), who favors sticking with a harder line that would force Clinton to veto the measure or alienate liberals by signing it.

There are also policy differences. Unlike the Senate measure, the House bill would deny new aid to children born to welfare mothers while allowing states to convert the federal

food stamp program into a cash grant. Both Senate and House versions also would deny public assistance, including food stamps, to legal immigrants.

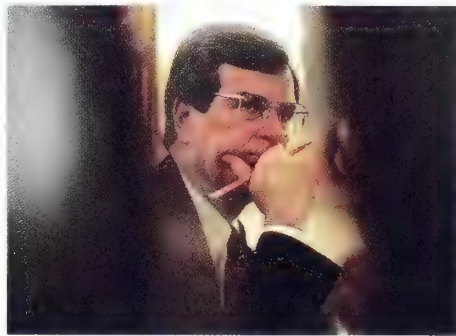
Clinton is facing pressure within his own party. Five Democratic senators, led by Daniel P. Moynihan of New York, on July 23 warned that without a veto, “We will have children sleeping on grates.”

In the end, strategists for both parties say it’s better to have a compromise than a breakdown that angers voters. Republican National Chairman Haley Barbour says reform “is good

for the American people. Hopefully, the President will sign the bill now.” And Michigan Governor John Engler, a state welfare reform pioneer, says the GOP should not block an overhaul just to deprive Clinton of a victory. “A signature doesn’t take the issue away from the Republicans,” he says. “We’re going to benefit from delivering on our promise.”

Indeed, a new welfare law could prove to be win-win for everybody—Clinton, Lott, Hill Republicans. Everyone, that is, but Bob Dole.

By Paul Magnusson and Richard S. Dunham



LOTT: “Do what’s right for the country”

CAPITAL WRAPUP

PULPIT POWER TO THE PEOPLE

► Organizers of the Aug. 12-15 Republican National Convention in San Diego plan to sell GOP gospel using “real people” instead of long-winded speeches by politicians. Among the ordinary citizens who will be trotted out are small-business owners who have battled burdensome regulation. “These are the real heroes of the fight for smaller government,” says one convention planner. Another likely speaker: an ex-welfare mother promoting GOP reforms.

McLARTY: MEXICO-BOUND?

► White House Counselor Thomas F. “Mack” McLarty III is a top choice to replace James R. Jones as U.S. Ambassador to Mexico if President Clinton is reelected, Administration sources say. McLarty, a Clinton pal since childhood, helped organize the 1994 Summit of the Americas and has since been an unofficial roving ambassador to Latin America. The Clinton confidant also is a top contender to head the Commerce Dept. should Secretary Mickey Kantor move on.

A RUN AT FANNIE AND FREDDIE

► House Banking Chairman James A. Leach (R-Iowa) is after mortgage giants Fannie Mae and the Federal Home Loan Mortgage Corp. again. Leach wants the highly profitable government-sponsored enterprises to pick up some of the tab for replenishing a nearly empty fund that insures thrift deposits. Friends of Fannie Mae and Freddie Mac, which buy home loans from thrifts and other lenders, argue Leach’s idea amounts to a tax on homeowners.

Meet the company that Meet Hoechst. *Who?*

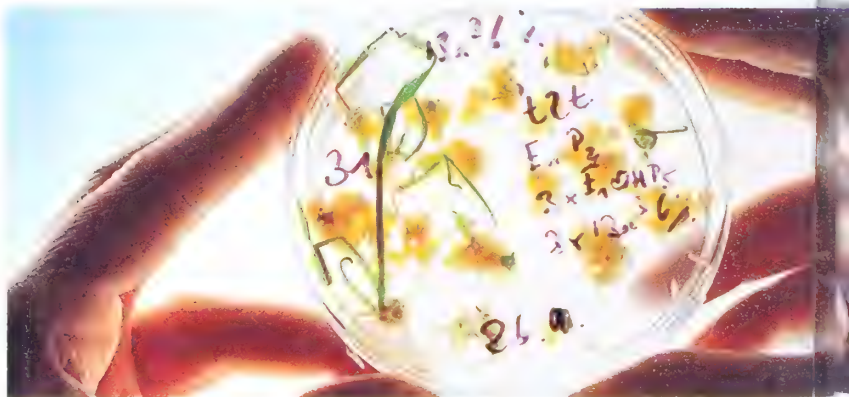
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BEVERAGES: Jianlibao seeks knowhow

For over half a century, Southwest Products Co. has supplied the U.S. defense and aviation industries. The small but highly regarded Irwindale (Calif.) company has carved out a niche as a leading manufacturer of spherical bearings for aircraft made by Boeing, McDonnell Douglas, and Lockheed. Today, its 60 factory workers make bearings for the Pentagon's C-17 military transport plane. NASA even uses Southwest's bearings in the Space Shuttle.

Figuring out just who owns the company leads to a tale of some complexity. Last January, a recently formed U.S. company named Sunbase Asia Inc. bought Southwest. But it is an American company only on paper. Although it's listed on NASDAQ, Sunbase's real owners are in Hong Kong and China.

In fact, Chinese government companies are among those owners. The key player is Genter Gao, a skilled dealmaker from the mainland, now in Hong Kong, who has valuable connections across China. His partner is New China Hong Kong Group, an investment fund

that includes some of Beijing's largest state-owned conglomerates. Sunbase also owns a huge bearing company in Harbin, a city in China's northeastern Rust Belt, still partially owned by the city government.

Clearly, Southwest's new owners wanted it for more than quarterly earnings. What they got was a company with solid U.S. government contracts and technology sensitive enough that Southwest needed U.S. government approval to transfer knowhow to a joint venture in Shanghai. Now, Southwest can help transfer some technology to Harbin. "We have the opportunity to take them to the next level," says former Southwest CEO



MILITARY INFLUENCE: The money

William R. McKay, an American who is now CEO of Sunbase.

Sunbase is a link in America's new China connection. It is one of hundreds, perhaps thousands, of companies with Chinese ties that have quietly stepped

China Inc. in America

Here are the different kinds of Chinese entities operating in the U.S.

STATE-OWNED ENTERPRISES Affiliates of central government such as Sinochem, CITIC, and COFCO have been active in real estate, manufacturing, and finance and are the largest direct Chinese investors in the U.S.

PROVINCIAL AND CITY COMPANIES Formerly obliged to work through Beijing, locals have now set up their own American trading, manufacturing, investment, and financial companies

PEOPLE'S LIBERATION ARMY COMPANIES Military-owned companies such as Norinco have a widespread network of American affiliates importing Chinese-made consumer goods, toys, auto parts, and medical equipment

HYBRIDS Working through wholly owned subsidiaries in Hong Kong, many companies are blending funding from Chinese government or military entities with Hong Kong capital, blurring their identity



999 brand pharmaceuticals, advertised in New York's Times Square, is partly owned by the People's Liberation Army

operations in the U.S. From gigantic state monopolies to nimble new enterprises backed by local municipalities, the Chinese corporate presence is spreading in myriad ways. A prosperous village in Shandong province now owns a 213-room hotel, the Cockatoo Inn, near Los Angeles International Airport. A company partially owned by the People's Liberation Army (PLA) advertises its 999 brand pharmaceutical products on a Times Square billboard.

ARK SIDE. Despite the ups and downs in relations between Beijing and Washington, the Chinese have lots of reasons to expand in America. Many see the growing \$35 billion trade surplus with the U.S. and want to get a greater piece for themselves. Others crave U.S. technology and capital to boost their campaigns to compete in China and elsewhere. Within 10 years, "we'll see a significant number of internationally competitive Chinese firms," predicts Barry Naughton, an economist at the University of California at San Diego.

But there's a darker hue to some

Chinese activity. In many cases, companies are testing the limits of U.S.—and Chinese—policies. At a time when many U.S. lawmakers and business and labor leaders worry about technology flows to China, Chinese entities operating in the U.S. are winning access to knowhow. Trade is another area of potential abuse. In May, U.S. representatives of PLA companies were among 14 people charged in San Francisco in an alleged scheme to smuggle AK-47 machine guns and other munitions into the U.S.

Moreover, an estimated 100 Chinese companies have employed sophisticated maneuvers to acquire listed companies in North America, gaining backdoor access to financial markets. If the practice expands, it could undermine the ability of regulators to maintain transparency and protect smaller investors.

The China connection thus is a double-edged sword. It can help introduce Western business concepts into China's economy. But it also means that Americans are confronting a new kind of foreign investment, sometimes made by compa-

nies that aren't really private. And the corporate model favored by Chinese companies is so complex, with multiple layers and various offshore entities as buffers, that it is often hard to determine the real ownership (table).

If current trends hold, this Chinese influx could be just the beginning. According to the new China Chamber of Commerce in U.S.A. Inc., fewer than 400 companies from China have approval from Beijing to be in the U.S. But it estimates the actual number is more than 1,000. Add companies run by Chinese nationals in the U.S. and the number is more than twice that, says Xiaomin Chen, a graduate of Brigham Young Law School who is president of the U.S.-China Lawyers Society.

Since only a tiny percentage of China's millions of enterprises are operating in the U.S., the potential for growth is huge. Many in Corporate America anticipate a spending spree. "They'll do what the Japanese did in the 1980s," predicts Robert S. Bodey, a senior manager at Deloitte & Touche in New York. "One



DRUGS: In New York, a Livzon unit will make aspirin for the U. S. market

day they'll get wired \$300 million [from China] and buy something." For a piece of that future business, Deloitte & Touche and eight other companies have formed the American Association for Chinese Companies (AACC), which helps mainland businesses get established in the U.S.

For Chinese companies starved for capital, perhaps the biggest attraction is U.S. cash. The process usually starts with forming a joint venture with overseas partners, often Hong Kong-based subsidiaries of Chinese outfits. That turns it into an overseas joint venture, beyond the reach of Beijing's regulators. The new company finds an American shell, buys out the old owners, changes the name and management, and starts doing business as a new U.S. company. Sunbase Asia, for instance, got its listing on NASDAQ through a reverse takeover of Pan American Industries Inc. last year.

As at Sunbase, American executives often head up these new companies. Joseph R. Wright Jr., for example, a former vice-chairman of W.R. Grace & Co., is the unlikely chairman of AVIC Group International Inc., a telecom company. AVIC's largest shareholder is Beijing Catch Communications, owned by the Beijing city government. Beijing Catch started AVIC last year to get capital for telecom projects such as paging and satellite networks. "We wouldn't do this if we weren't partially owned by the government," Wright says.

Technology is another powerful lure for Chinese entities. In an industrial park on the northern shore of Long Island, for example, Brian Z. Li runs a new subsidiary of Livzon Pharmaceutical group, a Guangdong drugmaker that is trying to soak up U.S. knowhow. Li, a Guangdong native who got a masters degree from St.

John's University in 1991, says the small plant started production of acetaminophen last month and will begin producing aspirin in September. The goal is to have a line of over-the-counter drugs for store brands of U.S. chains.

As he proudly shows off his new lab, Li says his main goal is "a very aggressive research and development program." To learn about developing new products as well as to follow strict U.S. safety standards for drugmaking, the company has hired a chemist, laboratory supervisor, production manager, and marketing specialist from other companies.

Like Livzon, more Chinese companies want to use expertise gained in the U.S.

to help their home business. Soft-drink maker Jianlibao America Ltd. in New York is in search of knowhow to take back home. Likewise, Shanghai Tire & Rubber Co. has an R&D center in Akron. Thanks to research conducted by local hires there, the company's Shanghai factories in June started rolling out radi tires for the first time. Now, General Manager Wang Dengxiang says he's trying to match rivals such as Goodyear Tire & Rubber Co. and Bridgestone Corp. "We have to speed up our technology development or we will have lost our opportunity," says Wang.

NOT SHY. Such talk worries some U.S. China-watchers. Chinese companies have a license from headquarters to acquire technology, says Ron Montaperto, senior fellow at the Institute of National Strategic Studies in Washington. Montaperto believes government and military companies may be getting some technology illegally. "They'll get it most any way they can," he says. So far, though, no Chinese have been convicted in cases involving industrial espionage.

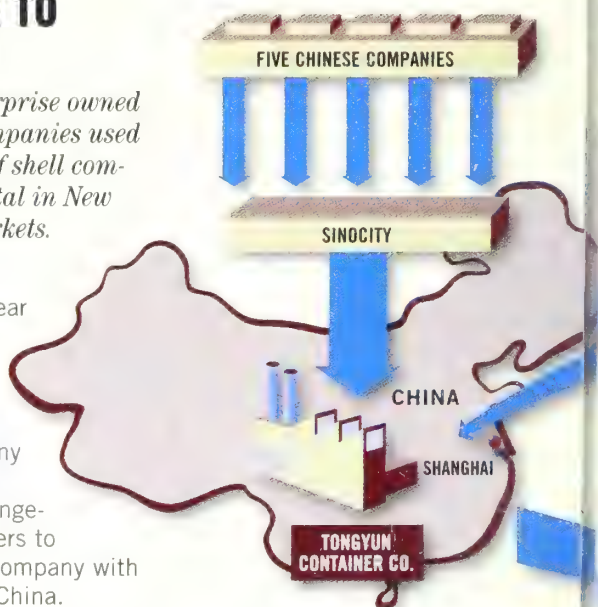
Of all the Chinese entities operating in the U.S., the most controversial are those owned by the People's Liberation Army. One of the biggest is China Norinco Industries Corp., or Norinco. With some 10 subsidiaries in California, Michigan, New Jersey, and elsewhere, Norinco is an active importer and exporter of sporting goods, medical equipment, auto parts, and other products. A Norinco subsidiary imports Chinese-made toy dogs and cats named "Spunky" and "Princess."

A BACK DOOR TO U.S. CAPITAL

Here's how one enterprise owned by Chinese state companies used a complex pattern of shell companies to raise capital in New York's financial markets.

THE ORIGINAL COMPANY

Tongyun Container near Shanghai is majority owned by a Hong Kong entity called Sinocity. But Sinocity is a front company for five Chinese state companies. This arrangement allows the owners to qualify as a foreign company with special privileges in China.



Other imports from China aren't so innocuous, according to the U.S. Attorney in San Francisco. Norinco employees in China and the U.S. were among those targeted after a U.S. Customs and Bureau of Alcohol, Tobacco & Firearms operation allegedly implicated them smuggling weapons into the U.S. Others charged included the president of Dynasty Holdings, a subsidiary of Poly Technologies, also with ties to the PLA. All defendants have pleaded not guilty, and no trial date has been set yet.

Even with such setbacks, companies affiliated with the Chinese military are expanding their U.S. business. Xinxing, run by another branch of the PLA, has a new trading company in El Monte, Calif. While the home company exports military and police uniforms to other countries, Xinxing (U.S.A.), which opened last year, sticks to imports of nonmilitary clothes for the American market, says a Xinxing manager in El Monte, who insisted on being identified only as Michael.

The network of PLA companies has expanded even as congressional critics of Beijing, having failed to cut off China's most-favored-nation trade status, have targeted PLA companies for sanctions. Representative Benjamin A. Gilman (R.-N.Y.), chairman of the House International Relations Committee, is planning to hold hearings this September on the PLA's role in the U.S. economy.

U.S. labor unions are also uneasy about the growing presence. AFL-CIO Secretary Treasurer Jeffrey L. Fiedler has started tracking PLA companies. "They're more aggressive, there's no question," he says. "You have American people as consumers unwittingly subsidizing the PLA."

But military-related players are a distinct minority. More typical is BNU Corp., a wholly owned subsidiary of state-owned China National Cereals Oils & Foodstuffs Import & Export Corp. (COFCO). It plans to break ground later this year on an \$80 million commercial retail, office, and hotel complex in Phoenix. Another subsidiary has issued \$150 million in commercial paper out of Chicago since 1994. The goal, says BNU's Chinese-born president, Elizabeth N. Mann, is "to make



STING: Are Chinese involved in smuggling arms?

COFCO a real multinational company."

That's the goal of many Chinese enterprises operating in the U.S.—to transform themselves into much more globally competitive companies. "It's hard to imagine a well-developed country without big, well-known companies," says Yang Hongwei, president of Beijing-owned Sinochem (USA) Inc., a conglomerate with ambitions to rival South Korean giants. "We want to develop into a company like Daewoo."

Chinese companies such as Sinochem are still only in the beginning stages of absorbing U.S. capital and knowhow. Likewise, many Americans are just now learning about China's expanding connections. For Americans who have finally learned to understand Japanese investment, China represents a different model. Japan's investments are led by its big *keiretsu*, or industrial groups. But with China, many investments are spurred by government-owned entities.

The U.S. could become a base that encourages entrepreneurial Chinese to push for economic liberalization

Ultimately, China's expanding connections in the U.S. could have an impact on how Washington manages overall relations with Beijing. The U.S. might lose some leverage in shaping the Chinese government's conduct on, say, human rights if state-owned entities and military-backed units are able to raise capital and win access to technology in ways that Washington can't control.

UNKNOWN. But it's also possible that a growing presence of Chinese companies in the U.S. could have a beneficial impact. American companies with big investments in China might not be so vulnerable to Beijing's scorn if Washington is able to retaliate against Chinese state-backed companies in the U.S. More broadly, the U.S. could emerge as a base that encourages the most entrepreneurial Chinese to push for economic liberalization. By moving into the U.S., these companies are forging closer ties between the two countries, ensuring a greater exchange of ideas and expertise.

No one can predict yet whether the expanding China connection will be a long-term force for better or worse. But it is destined to grow rapidly and touch many sectors of the American economy. Ever since China opened to the U.S. in 1979, American leaders have talked about how U.S. business investment will help transform the Middle Kingdom. The scale is smaller, for sure, but the Chinese are starting to show that they can have an impact in the U.S., too.

By Bruce Einhorn in New York, with bureau reports

THE NEED FOR CAPITAL Facing bureaucratic obstacles to listing on China's stock exchanges, the company decides to raise capital in the U.S.



THE HOLDING COMPANY Through Sinocity, the Tongyun investors take an 80% stake in China Container Holdings (CCHL) in the British Virgin Islands, a tax and regulatory haven.

THE REVERSE TAKEOVER To avoid the cost and difficulty of a direct listing in New York, the British Virgin Islands company merges itself into a moribund publicly traded U.S. company. It changes the name to China Container Holdings (U.S.A.). This entity issues shares and funnels capital back to Tongyun in China.

(DATA CCHL U.S.A.)

INDIA

A TRAFFIC JAM OF AUTO MAKERS

They're pouring in money as others jump into the fray

At the Premier Automobiles Ltd. (PAL) factory on the outskirts of Bombay, there seems to be no end to the problems. The 25-year-old plant, where France's Peugeot has had a joint venture with PAL since last year, is six months behind schedule in producing Peugeot 309s, a \$13,500 sedan. Provoked by a militant union leader, the workers are on strike, and production has come



to a halt. Some 500 new cars sit unsellable on the factory grounds, all with missing or wrong parts. Jacques Manlay, deputy managing director at the plant, is bewildered by the situation. "Everything is an opportunity to waste time," he says wearily.

JUST TWO. Peugeot is not the only frustrated auto maker in India. In the past two years, nine of the world's major producers, including General Motors, Ford, Fiat, Daewoo Motor, and Mercedes-Benz, have raced into India's newly opened car market. Lured by India's huge potential for growth, they now find themselves on a bumpy road. Fierce competition, labor trouble, a lack of suitable partnerships, high taxes, and infrastructure problems are just some of the hazards.

Despite the difficulties, the current players are putting more money into India even as other foreign makers, led by South Korea's Hyundai Motor Co., are planning to jump into the fray. With so many producers crowding into a market ill-equipped to support them all, the stage is set for a shakeout.

The key to who wins and who loses could be how fast a company can offer models in the small-car segment and how quickly it can achieve fully integrated manufacturing operations, complete with parts suppliers. That seems to favor the bigger, more aggressive players such as Ford Motor Co. and Daewoo Motor Co.

For 35 years, Indians had a choice of just two cars: a clunky 1954 Morris Ox-

'TOUGH PLACE'

A Ford plant in Nashik, India, and a Peugeot showroom in Bombay. Foreign auto makers have been plagued by labor troubles, and the higher-priced models they've focused on aren't selling



ford or a 1951 Fiat, made by Hindustan Motors Ltd. and PAL, respectively. Then, in 1984, a joint venture between the Indian government and Japan's Suzuki Motor Corp. gave the auto market its first taste of competition—an 800cc people's car, the Maruti, the most popular car in India today. But after deregulation in 1991, competition picked up as foreign makers started filling showrooms with sleek models.

Hoping to get off to a fast start, most of the new entrants made their debuts not in the mass market, where 70% of Indian car sales are concentrated, but in the premium segment. They rolled out

cars with engines bigger than 1000cc and price tags above \$11,500. This has turned out to be too pricey for most Indian consumers—it's 16 to 24 months' average salary, compared with the six months' income that Americans pay for their cars. General Motors Corp.'s Opel Astra recently hit the roads at a price of \$20,000.

Partly as a result of that mismatch, sales targets are falling short. Mercedes with a \$63,000 price tag for its E220 model, has an annual production capacity of 20,000 cars but has sold just 600 so far. Fiat expected to sell 15,000 Unos in 1992 but has sold just 380, in part because of labor troubles at joint-venture partner PAL. "The market is not expanding rapidly as the number of entrants come in and making cars," says Hormis Sorabjee, associate editor of *Auto India*, India's leading auto publication. "It's a tough place to operate."

The foreign auto makers are finding that one of India's biggest attractions—cheap and abundant labor—can be a major problem. Labor relations in India have long been acrimonious. In the past two years, three of India's major car makers, two of whom have foreign partners, have suffered crippling strikes. The

most recent was at a PAL Bombay plant that assembles Fiat Unos. The labor troubles have left managers and workers apathetic, and productivity is dismal. Against a global standard of 40-plus cars per worker per year, India makes an average of five.

The foreign makers are trying to improve relations with workers and unions. Ford, GM, and Daewoo provide rigorous training for their workers and even send some overseas to learn about internationally prevailing workplace practices.

The companies also are trying to refine their manufacturing strategies. Mindful of the problems of maintaining quality in

India, most started out by importing car kits to assemble rather than setting up full-fledged manufacturing operations. But that approach as its own hazard, because importing components is expensive. Duties are a prohibitive 10%, and even a single replacement screw can take a month to arrive.

Finding independent local suppliers is tricky. Only a few in India could meet the exacting standards of a Ford or a Daewoo. Beyond that, the successful component makers all have alliances with Suzuki's Maruti Udyog. The competition is so savage, say some analysts, that Maruti has threatened to cut off suppliers from their Maruti 800 contracts if they accept other business. The company denies making such threats.

NEW PLAYERS. But the message is clear: To have a high-quality, cost-competitive parts network, you have to build it yourself. That's why carmakers including Ford have asked their European suppliers to come to India and set up parts-making joint ventures with local companies. GM's component subsidiary, Delphi, already has set up shop in New Delhi to service the Opel with imported and locally made parts.

The competition will only get fiercer. Five other new players will enter the Indian market this year. Hyundai plans to build a \$1.1 billion plant, and Mitsubishi, Volkswagen, Toyota, and BMW also are jumping in. Waiting still is Chrysler Corp., which has been looking for a suitable partner for a year. So far, more than \$3.5 billion of investment has been planned, and showrooms glitter with new models the likes of which India has never seen.

The survivors will be those that can successfully make an 800cc or smaller mass car, predicts S. G. Shah, adviser to the Association of Indian Automobile Manufacturers. This segment is where Suzuki is king. Priced at \$7,000, its Maruti 800 accounts for 65% of all Indian car sales. So far, none of the new entrants has attempted to cross swords with the Maruti, but Ford, Daewoo, and Indian truckmaker Telco all have plans to manufacture small cars in the future.

Is there room for them all? Some experts question whether India's crumbling infrastructure can support the furious pace at which new cars are hitting the roads, a rate of 900 every day. Streets are in such a dismal state that of the

The Foreigners Driving Into India

COMPANY	LOCAL PARTNER	MODEL	INVESTMENT	ANNUAL PRODUCTION
DAEWOO MOTOR	DCM	Cielo	\$1 billion	72,000
FORD MOTOR	Mahindra & Mahindra	Escort	\$800 million	20,000
PEUGEOT	PAL	309	\$200 million	20,000
MERCEDES-BENZ	Telco	E220	\$100 million	20,000
GENERAL MOTORS	Hindustan Motors	Opel Astra	\$91 million	12,500
FIAT	PAL	Uno	NA	15,000
MITSUBISHI	Hindustan Motors	Lancer	\$70 million	10,000
SUZUKI	Indian govt.	Maruti line	\$450 million	100,000

DATA: BUSINESS WEEK

1.5 million miles of roads in India, just 20% are car-worthy. Although the government plans to build an additional 30,000 miles of road, the estimated cost is an astronomical \$142 billion.

So far, the answer seems to be that Indians will buy the cars even if the roads aren't ready. For the past three years, growth in car buying has averaged 25% annually. Despite high taxes amounting to almost 50% of a car's retail

price and one of the world's most expensive markets for fuel, at 69.4¢ a liter, "the impulse isn't slowing down," says Shah. India now produces 330,000 cars a year.

The market potential is huge. "India will be a major market in the 21st century," says John Parker, president of Ford India, which has an \$800 million investment and hopes to use India as an eventual export base. At 3.6 automobiles per 1,000 people, Indian car ownership is among the world's lowest. The

U.S. boasts 560 cars per 1,000. At least 2 million Indian households can buy a car with six months' wages. By 2000, provided economic growth is maintained at 6% to 7% a year, demand for passenger cars could reach 2 million units annually, some estimate. Those are the numbers that keep foreign investors plugging away, hopeful their day will come.

By Manjeet Kripalani in Bombay

EUROPE

TINSELTOWN ON THE THAMES

A filmmaking renaissance is sweeping Britain and the Continent

London's Pinewood Studios Ltd. is bustling these days. But the cast and crew are not making just arty British films in the tradition of such classics as *Kind Hearts and Coronets*. No, Pinewood has gone Hollywood. Or maybe it's better to say Hollywood has gone Pinewood. The studio is filming a \$46 million blockbuster, *The Saint*, starring Val Kilmer, for release next year by Paramount. Work on *The Saint* started soon after completion of Paramount's *Mission: Impossible*, the Tom Cruise hit also made at Pinewood.

Europe, for years an also-ran in film production, is fighting to emerge as a viable alternative to Tinseltown. Yes, government handouts still prop up some European film shops. But Europe, led by the British, is pressing its advantages in



SETTING UP A SHOT FOR CHANNEL FOUR'S TRAINSPOTTING

costs and plentiful talent. With the strong dollar buying more in Europe, U.S. movie studios including Warner Bros. Inc. and Paramount Communications Inc. plan to shift more production across the Atlantic. And European companies such as the

Anglo-Dutch PolyGram, Germany's Bertelsmann, and France's Canal Plus are putting more resources into their own film operations. The goal: "To beat Hollywood at its own game," says Michael Kuhn, president of four-year-old PolyGram Filmed Entertainment.

An exchange-rate swing could certainly slow this revival. But fortunately, a lot more local capital is pouring into the business, especially in Britain. The gradual deregulation of Europe's TV market has spawned a throng of new commercial

International Business

channels, which are spending more freely on film production. Britain's Channel Four is a champion in this area, having backed such winners as *The Crying Game* and 1994's *Four Weddings and a Funeral*—Britain's highest-grossing film ever, at \$250 million. Channel Four also provided the \$2.5 million budget for *Trainspotting*, a black comedy about Scottish heroin addicts that's now playing to packed art houses in Britain and the U.S.

Hot for more such successes, six of Britain's largest independent TV stations announced in mid-July a cooperative venture to make at least 10 feature films a year over five years. The number of British-produced or co-produced films jumped to 76 last year, from 40 in 1992.

Across the Channel in France, TV

portion of revenues on film production.

Adding to the hope for a turnaround is Hollywood's discovery that in Europe, costs are often lower (table), and stage workers and actors can be less demanding. "Our biggest advantage now is that U.S. prices are out of control," says David Puttnam, former head of Columbia Pictures and now a producer in his native Britain. Puttnam estimates that labor costs, which can eat up half a film's budget, are 30% lower in Britain than the U.S. In turn, the influx of foreign films shot in Britain helped boost total film investment there by 85%, to \$516 million in the first half of 1996, according to industry newsletter *Screen Finance*.

While most of the big studios are in Britain, the Continent remains popular

TV studio. It's planning a similar theme park and studio in Germany. At Walt Disney Co., 150 animators in a studio outside the Euro Disney theme park outside Paris worked on *The Hunchback of Notre Dame* and have now turned to *Hercules*. Last year, a Malaysian-backed group opened Third Millennium Studios on an old Rolls Royce aerodrome site in Britain. *Goldeneye*, the latest James Bond movie, was filmed there.

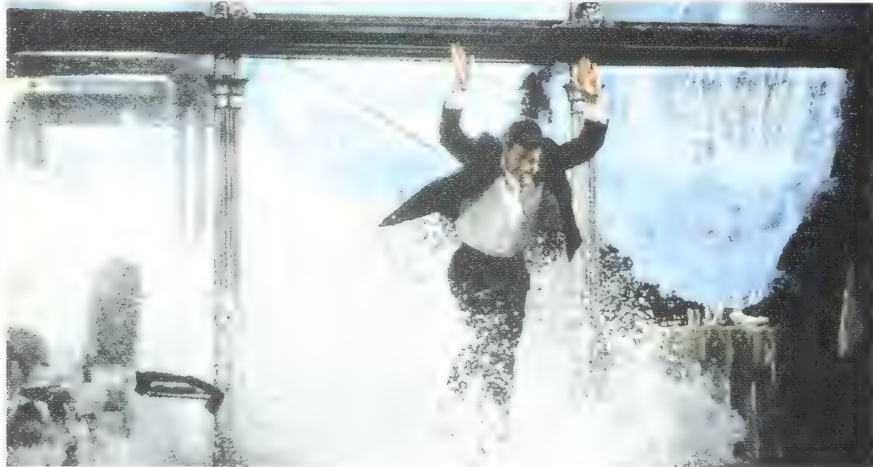
ON THE PROWL. The boom is luring some European directors back from Hollywood. Late last year, British directing brothers Ridley Scott (*Blade Runner*, *Alien*) and Tony Scott (*Top Gun*, *Crimson Tide*) paid \$19 million for ailing Shepperton Studios in London, aiming to turn it into a studio for blockbuster action movies. The Sec-

MISSION: IMPOSSIBLE'S Tom Cruise at Pinewood
are also part of a joint venture to create a European rival to George W. Lucas Jr.'s Industrial Light & Magic. Based in London's Soho district, Mill Digital Film Co. hopes to be fully running soon.

Meanwhile, several European companies want to join the Hollywood leagues. Most ambitious is PolyGram, an Anglo-Dutch media company that has so far invested more than \$700 million in its Los Angeles-based film unit, which worked with Channel Four on *Four Weddings and a Funeral*. Even though PolyGram Filmed Entertainment lost out to Kirk Kerkorian's \$1.3 billion bid to buy MGM/UA film studios in mid-July, Kerkorian says he's still on the prowl for acquisitions. Startup costs are still hurting results, though, despite such other successes as *Fargo* and *Dead Man Walking*. On July 24, PolyGram reported that the unit lost \$22 million on sales of \$407 million in the first half of 1996.

France's Canal Plus is still smarting from losing ventures in the U.S., including a 17% stake in bankrupt Carolco Pictures Inc. Pulling back from the U.S., it is focusing instead on production agreements with three French studios for such films as *Assassins*, a psychological thriller from the hot young French director Mathieu Kassovitz. Canal Plus also has a joint venture with Sony Corp. in Britain to produce two or three English-language films a year. "In France, for a long time it was enough to make critics rave," says Brahim Chioua, co-operating officer of Studio Canal France, the company's film production unit. "We're paying more attention to commercial success." That attitude may finally nurture a vibrant film industry.

By Julia Flynn, with Katherine Miller in London, and bureau reports



Production Costs

	CAMERA RENTAL Weekly rate	PRODUCTION MANAGER Weekly wages	CHIEF ELECTRICIAN Weekly wages	EXTRAS Daily rate
HOLLYWOOD	\$13,285	\$3,518*	\$1,504*	\$99
LONDON	\$5,766	\$2,712**	\$2,325**	\$87

For a 5-day week

DATA: BRITISH FILM COMMISSION, HYDRA ANALYTICS

funding for feature films reached a record high last year and accounted for more than a third of the \$529 million invested in French films. Germany's ZDF, a national public broadcasting network, has boosted its spending on feature films by 50%, to about \$67 million, since the late 1980s. What's more, with the advent of digital television, Europeans soon will be receiving hundreds of channels on their sets. As a result, analysts predict that demand for feature films could expand further. "In a competitive market, having your own product is an important edge," says Richard J. Turner, head of the media consultancy practice at London Economics. The trend is helped by the requirement of some European governments that local TV stations spend a

portion of revenues on film production. This spring, the streets of Budapest were transformed into 1950s Buenos Aires for the filming of *Evita*, starring Madonna and directed by Britain's Alan Parker. And Sylvester Stallone, who boosted the local economy by spending \$3,500 a day on his hotel room, recently wrapped action flick *Daylight* in Rome.

Hollywood is doing more than just renting sound stages. In March, Warner Bros. set up a state-of-the-art London animation studio to use Europe's ample talent in this area. It hired 85 local animators, including Russell Hall from *Who Framed Roger Rabbit?* Warner is also joining with entertainment group MAI PLC to build a \$350 million theme park in rural Britain that will include a film and

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A GREAT SLIDE BACKWARD IN SOUTHEAST ASIA

When he presided over a landmark meeting of Pacific Rim heads of state in 1994, Indonesia's President Suharto was hailed as a dynamic advocate of free trade and modernization. But the Suharto who hosted a series of meetings of the Association of South East Asian Nations (ASEAN) in late July came off more like a run-of-the-mill dictator. As the meetings droned on in Jakarta, thousands of protesters assembled across town to jeer the government's efforts to suppress an opposition party. And the would-be free trader was taking heat from Tokyo and Washington for allowing his son to set up a cushy car venture.

As his health declines, Suharto, 75, seems obsessed with tightening his family's hold on the nation's wealth. Such behavior is very much in vogue in Southeast Asia today. After roughly a decade of economic reform and political liberalization, several countries are backsliding. That clouds the outlook for these nations, which have long been the darlings of investors.

In Thailand, the scandal-plagued government of Banharn Silpa-Archa is undoing much of the economic and political reforms put in place earlier.

In Malaysia, the government of 70-year-old Prime Minister Mahathir Mohamad has been privatizing everything from the national airline to the telephone service—but most of the spoils are going to cronies.

CELLAR GROWTH. There are signs that the penchant for money politics could hamper these countries' efforts to shift to more sophisticated export industries. While export growth is still high, it has declined dramatically in Indonesia, Malaysia, and Thailand, which is running a ballooning trade deficit. Of course, the ASEAN countries are making strides in some areas. They are slashing tariffs, and their 8% average growth rate remains the envy of the world.

But critics are saying that the failure to rein in corruption and coddled cartels is starting to take its toll. "Growth is unsustainable if your economy is not based on a high degree of competitiveness," says Jakarta-based business consultant Laksamana Sukardi. He figures that corruption adds up to 30% to the cost of doing business in Indonesia.

Technocrats and foreign investors worry that these countries just aren't taking the steps in such areas as education, labor relations, and investment regulations that are a must to move to the next level of development. Resources needed for education and infrastructure projects are being siphoned off in sweetheart deals for cronies and relatives.

This is already hurting some countries. Ford and General Motors recently called off major expansions in their Indonesian auto assembly operations after Suharto gave big breaks on duty and taxes to his son's auto venture with South Korea's Kia Motors. In Thailand and Malaysia, foreign electronics manufacturers say that a growing shortage of educated workers is becoming a constraint.

But the region's aging autocrats aren't getting the message. A defensive tone emerged from the Jakarta sessions. The ministers vowed to resist efforts by the West to discuss corruption, environmental woes, and labor abuses at the World Trade Organization. Shrugging off Western objections, they also embraced the harsh regime in Burma as a prospective ASEAN member.

How stiff a price Southeast Asia will pay for stagnant leadership remains to be seen. Much of the world would love to have its problems. But glaring political and social ills are starting to hurt prospects.

*By Pete Engardio in Jakarta,
with Robert Horn in Bangkok*



IN JAKARTA: More cronyism than leadership

GLOBAL WRAPUP

RUSSIA'S BANK SHAKEOUT

With President Boris Yeltsin safely reelected, the central bank is finally showing signs of getting serious about dealing with the troubled banking system. It recently closed over Universal Bank, one of Russia's larger financial institutions, with \$1.2 billion in assets. This is the first time the government has closed a major private bank. The central bank blasted management for making risky real estate investments.

A major shakeout in the banking in-

dustry could soon follow. With some 2,100 financial institutions, Russia is widely considered overbanked. Many of these have severe problems. Over the next few months, many of the smaller banks are likely to be shut down. The government will try to keep larger banks afloat, however, perhaps by taking over their management.

DOGFIGHT OVER FRANCE

► French skies should be the scene of the most vicious dogfights as Europe's airlines brace for total deregulation next Apr. 1. Already,

British Airways PLC is moving in on the French market, Europe's biggest, as BA's vulnerable rival, Air France, fights a losing battle to boost productivity. On July 23, BA paid \$32 million to purchase the 50.1% it didn't own in TAT, a domestic French carrier. It also hired a new chairman for TAT, which has lost money every year since BA bought a stake in 1993. Feisty French carriers, including Air Liberté and AOM French Airlines, are also nipping at Air France. The likely result: falling fares, red ink, and an eventual shakeout.

All roads lead to Milan.



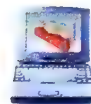
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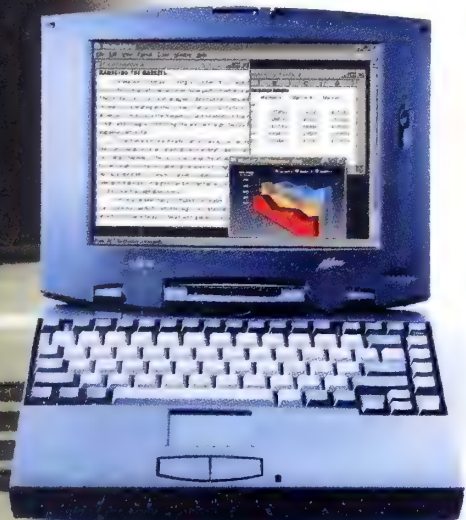
supported by this philosophy—in the use of quality components, in precision manufacturing,

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ARE PROFITS SHAKIER THAN THEY LOOK?

Slowing cash flows may be a sign of widespread trouble

When news leaked out early in July that a key cash flow measure at AlliedSignal Inc. appeared to be deteriorating sharply, officials at the Morristown (N.J.) industrial giant rushed to sound a reassuring note. Sure, Chairman Lawrence A. Bossidy had sent out a tough memo only weeks earlier warning his managers to watch their cash outlays. The memo came after Allied's internal projections showed that free cash flow—cash from operations left over after dividends and capital expenditures other than acquisitions—would tumble to a negative \$134 million for the half.

But Allied was quick to argue that there was no cause for concern. It dismissed the problem as temporary, since the capital spending and inventory buildup needed to fuel Allied's strong sales growth comes early in the year, while cash pours in during the second half when customers pay for big orders. And on July 22, when Allied reported a 16% gain in net income for the second quarter, excluding special items, it announced that by tightening ship, it had already cut the free cash shortfall to \$90 million. For the year, free cash flow should hit \$300 million. "There's no problem with cash flow here," says a spokesman.

Ask Jeffrey D. Fotta, president of Boston's Ernst Institutional Research, what he makes of that explanation, and he lets out a whoop. Fotta earns his living searching for signs of trouble or turnaround in the quarterly cash-flow statements offered up by Corporate America—and he has had Allied on his hit list since mid-1995.

JITTERY STREET. Why? Fotta argues that Allied's growing sales and earnings mask a serious problem. Over the past year, the rush to boost sales has left Allied with deepening difficulty in meeting its cash needs from operations. "They're growing too fast and not getting the returns from capital investments they used to," says Fotta. "Allied peaked in mid-1995, and returns have been deteriorating since." Without major changes, he

predicts, AlliedSignal will have increasing difficulty keeping up its double-digit earnings growth.

Allied may not be alone. After four years of spectacular profit growth, questions abound concerning the stability of Corporate America's earnings. With Wall Street jittery and the Federal Reserve's direction uncertain, confusion has spawned a worried search for signs that the momentum behind profits is slowing. And two key indicators of earnings strength—operating and free cash flows—are clearly flashing yellow.

Even as Corporate America's sales and earnings continue to advance, Fotta and others who closely track cash see slippage. "Companies have worked extremely hard to cut corporate fat throughout the recovery, and that has generated great cash flow," says Jason J. Wallach, senior portfolio manager for Systematic Financial Management, an investment firm that picks stocks based on cash flow. "But with earnings peaking, free cash flow is starting to deteriorate." For the four years ended in fiscal 1995, for example, free cash flow for Standard & Poor's industrials jumped an average of nearly 17% annually. But so far, for the four years ending with fiscal 1996, free cash flow is up just 8.2%.



The most worrisome sign comes from a regular screen of companies in the Russell 1000, an index of the U.S. largest-cap stocks, done by Fotta. Using an adjusted measure of operating cash flow (OCF) devised by his firm (but Fotta tracks changes in quarterly cash flows. The latest news isn't good. When Ernst's measure of OCF was growing 80% of the Russell companies 12 months ago, the proportion has dropped steadily since. Today, OCF is falling at 55% of the companies. "That's a fundamental sign that things are not healthy. Last time they looked this bad was early 1990," says Fotta. "A lot of companies are not in as good shape as people think."

As with Allied, the main culprit appears to be cyclical overexpansion. That could mean trouble ahead, since changes

HOW THIS BEAR CRUNCHES THE NUMBER

Most cash-flow sleuths looking for companies in trouble begin with operating cash flow. But cash-flow specialists at Ernst Institutional Research in Boston have gone a step further.

Using a technique known as dual cash-flow analysis, which compares the cash a company is getting from operations with cash coming from its balance sheet, they can often spot signs of deteriorating fundamentals well before traditional cash-flow analysts can. "If we

see a fall in operating cash flow, and with an abrupt shift in the way a company manages its balance sheet, it's a sign that management sees trouble ahead," says Ernst President Jeffrey Fotta, whose tiny firm provides research to the likes of Fidelity Investments, Signet Banking, and other institutions.

One recent success: By watching buildup in capital expenditures and inventories throughout the semiconductor industry even as many companies

A JEFF FOTTA TIP SHEET

By comparing cash flow from operations with cash from the balance sheet, Jeffrey Fotta's "dual cash flow" model may spot problems months before they show up in earnings or in conventional operating cash-flow analysis.

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UNFAVORABLE

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Intel
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Toys 'R' Us
Microsoft
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Alcoa

INDUSTRIES

Beverages
Pharmaceuticals
Oil

Autos
Paper
Semiconductors
Steel

DATA: ERNST INSTITUTIONAL RESEARCH

As a result, Ernst's operating-cash-flow figures for Allied turned negative by spring 1995. Since then, says Fotta, Allied hasn't met its cash needs from operations and has increasingly turned to balance-sheet maneuvers such as drawing down accounts receivable instead. "They've invested money but aren't getting returns out of it," he says.

Allied hotly disputes that contention. "It's not an accurate overall picture of the quality of our cash flow," says a spokesman. But if Fotta's methods are con-

amortization, and by the timing of when they book sales or expenses. Such finagling is far harder with OCF, so it's the first place trouble shows up. "When a company starts to see a downtrend in cash flows, poor profits will likely follow," says Howard M. Schilit, an accounting professor at American University in Washington who specializes in detecting gimmickry in corporate reporting.

Yet to Fotta, even the way receivables and payables are accounted for offers executives room to maneuver. So, unlike most analysts, he also removes them from OCF. By doing so, he can pinpoint binds of the sort that he says AlliedSignal faces. As demand has soared for its goods since the early 1990s, Allied has poured money into capital spending, new equipment, and inventories. But according to an analysis of dual cash flow done by Fotta's firm, the higher sales Allied has gained from the buildup haven't offset the increased costs they've added. Growth rates for Allied's return on sales—measured by retained earnings added to shareholders' equity—are dropping, not increasing.

troversial among companies he covers, they've won fans among investors. "He's a trailblazer; he allows you to catch turning points in stocks," says Garry M. Allen, president of Virtus Capital Management, the money-management unit of Signet Banking Corp. "It's so easy to distort earnings, but this offers a much closer sense of the underlying cash-flow dynamics."

Indeed, Fotta's screens are turning up a surprising number of warning signs at companies that otherwise look healthy. Although Merck & Co. just posted a 13% hike in second-quarter profits, it, too, is on Fotta's don't-touch list. The problem again is over-investment. Merck, he argues, has steadily increased capital spending and inventories, but gains in Merck's OCF, as measured by Ernst, are slim. The capacity is adding little growth to retained earnings. Merck refused to comment.

General Motors Corp. appears headed for trouble, too. With growth rates for sales and retained earnings falling fast, Ernst's measure of operating cash flow growth is tumbling. Yet GM is piling on capital spending and inventory. GM argues that its returns have been temporarily hurt by a strike early this year, as well as by a nonrecurring charge it made to fund its pension plan. Another reason is the heavy long-term spending it's making to fuel foreign growth. "That's not investment that gets a 12-month payback," says a high-ranking GM financial executive. "I'd have trouble saying we're not getting returns on our investment."

But Fotta believes that "GM is growing right into its problems. It's adding liabilities to make up for operating cash-flow shortages—not a healthy thing to do when sales and earnings growth are dropping." It could be one more sign that behind strong numbers, bad news can sometimes lurk.

By Jane A. Sasseen in New York

cash flow tend to precede changes in earnings by several quarters. Case in point: Hewlett-Packard Co. After it learned on July 11 that poor third-quarter sales mean it's unlikely to meet analysts' earnings estimates, the stock tumbled. Anybody watching its OCF had a lot of future woe. In mid-1995, HP's operating cash flow fell from its normal level of more than \$600 million to just \$2 million combined for the second and third quarters.

Why the lag? While both income and cash flow figures measure underlying operating performance, companies have more wiggle room in how they report income. Under generally accepted accounting principles, managers in a bind have plenty of ways to massage income through "non-cash" items such as depreciation and

falling OCF, Ernst warned away from chipmaker stocks in 1995, well before recent earnings problems surfaced.

Why does dual cash-flow analysis work? The biggest difference between dual and standard cash-flow analysis is where the numbers are defined. Unlike conventional measures, Ernst counts cash flow in accounts payable and receivable as part of balance-sheet cash flow, not operating cash flow. That's because those numbers can be manipulated: Management has lots of leeway stretching out payments or accelerating collection of its receivables. As returns from sales start to

slow down. "Management only has so many levers to pull when they hit trouble," says Fotta. "It's the first place they turn for cash."

Using those reworked numbers, Ernst then creates a number comparing operating cash flow with balance-sheet cash, which it calls dual cash flow. When dual cash flow is positive, that means a company is meeting its cash needs from operations. When dual cash flow turns negative, the company is turning to debt or other balance-sheet maneuvers for the cash it needs. That may be sustainable in the short term—or in periods of strong growth—but it can't last forever.

RYDER SEES THE LOGIC OF LOGISTICS

Its main thrust will be planning transport for others

Ryder System Inc.'s signature yellow trucks were conspicuously absent from a technology exhibit at Miami's Doral Ryder Golf Tournament in March. It was a hint of things to come. On July 19, three days before reporting disappointing second-quarter earnings of \$31.6 million, Ryder CEO M. Anthony Burns, 53, announced plans to sell off the company's struggling consumer truck-rental unit. It was the latest of Burns's efforts to focus Miami-based Ryder on logistics—the organization and transportation of companies' supplies and products. Today, logistics makes up 17% of Ryder's \$5.1 billion in sales, with revenues growing at 30% annually.

Wall Street, which had for a long time advocated the shift, approved—even though the stock barely budged from the mid-20s, where it has been mired for three years. "[The sale] frees up capital to pursue greater growth opportunities," says Michael F. Baxter, a portfolio manager at Hotchkis & Wiley, which holds 4.3% of the stock. Still, Burns knows that betting the farm on the highly competitive commercial logistics business is a big risk. "My credibility is at stake," he says.

NO PAYOFF. He didn't have much choice. Ryder, long a force in consumer truck rental, had been caught in a brutal spending war with privately held U-Haul International Inc. Starting in 1993, Burns spent some \$200 million a year on trucks, systems upgrades, and a central reservations system. Yet the payoff never came: The unit's 1995 pretax earnings were \$10 million on sales of \$547 million, down from 1994's earnings of \$27 million.

Ryder's bright spot has been its logistics division, which should hit \$1.2 billion in sales this year, up from \$416 million in 1991. As corporate downsizing has increased, companies have

rushed to outsource logistics—and Ryder has seized the moment. In 1994, Burns bought LogiCorp, an Ann Arbor (Mich.) company that processes shipments for global carriers, for an estimated \$20 million. LogiCorp helped Ryder design sophisticated systems and gave it many new customers. "It was the best acquisition we ever made," Burns says.

Here's an example of why: Previously, LogiCorp did freight-rate analysis for United Technologies Automotive. Now, Ryder is managing inbound supplies for United Technologies Automotive's car-interiors plant in Port Huron, Mich. This fall, it will start managing logistics for nine additional UT plants. In late 1994, Ryder beat out 18 rivals for Whirlpool Corp.'s inbound logistics business, which moves parts from some 900 suppliers to 11 plants. The deal has also boosted Ryder's global reach: Recent contract wins include a Brazilian Pepsi bottler and a unit of Volkswagen.

Such success stories have helped make Ryder the largest player in the logistics game. Yet in some complex contracts, there have been glitches. Most notable is a \$70 million contract with OfficeMax, in which data-entry problems mixed up payments to carriers of merchandise. OfficeMax won't comment. Burns acknowledges problems but says they've been fixed. Whirlpool, too, hasn't yet met additional cost-savings goals stipulated in the Ryder contract. This has affected Ryder as well, since a "gain-sharing" contract lets it share in the savings.

Competition is heat-



"MY CREDIBILITY IS AT STAKE"

A dogfight with U-Haul left CEO Burns little choice but to ditch consumer truck rentals

ing up, too. With the logistics market expected to hit \$50 billion by 2000, from an estimated \$16 billion this year, players such as Schneider Logistics and CSX Corp. have joined the fray. Competitive pricing means that the revenues have outpaced profits. Last year Ryder took a haircut on margins to obtain a contract with General Motors Corp.'s Saturn.

SHIFTING UP. To boost margins to 10% by 1998, Burns has embarked on a cost-cutting campaign and has raised spending on information systems. Already Ryder's pretax logistics margins have more than doubled this year, to 45%, thanks to better pricing, greater contract selectivity, and more gain-sharing.

Can Burns keep Ryder trucking? Skeptics cite his poorly timed diversification into insurance and aircraft leasing in the late 1980s—just as both industries slumped. Burns then pared Ryder down to leasing, renting, and servicing truck—slow growth businesses, all. Says R. Schlesinger, an analyst at Donaldson Lufkin & Jenrette Securities Corp.: "The perception of the success of the last 10 years depends on having the logistics payoff realized." Translation: It's time to kick into higher gear.

By Gail DeGeorge in Miami

RYDER SHIFTS GEARS

- Puts its struggling consumer truck-rental division on the block
- Focuses on logistics through its deals with Whirlpool and others
- Strengthens its margins by cost-cutting, improved bidding, and sharing the cost savings with customers

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REGULATORS

HIS NAME IS MUD TO LLOYD'S U.S. 'NAMES'

Many of the investors see Phil Feigin's deal as a betrayal

To many Americans facing financial ruin in the wake of the Lloyd's of London meltdown, Philip A. Feigin is a traitor.

This is a far cry from last month, when the little-known Colorado securities commissioner was their hero. A veteran defender of ripped-off investors, Feigin led a team of state regulators who had rushed to the aid of the Americans embroiled in the Lloyd's debacle. Their strategy, as local law enforcers, was to sue the London institution in their home states for securities fraud.

The suits alleged that Lloyd's—which was trying to collect about \$275 million from 2,700 U.S. investors after a string of earthquakes, hurricanes, and other disasters—had broken state laws by failing to disclose the extent of its losses when it recruited them. To these American “names,” who had pledged their personal assets to back Lloyd's insurance policies, the local authorities, who had set up an advisory commission headed by Feigin, were their best hope of avoiding the crushing bill.

But Feigin's settlement fell far short of their expectations. He persuaded Lloyd's to reduce the Americans' liability by 23%, but in exchange dropped the state securities fraud suits. The names insisted that Feigin had assured them they wouldn't have to spend another penny. Attacking him as a grand-standing bureaucrat, they claimed he had gotten in over his head. “He was hoodwinked. He must not have understood the meaning of the agreement he reached with them,” says Richard Rosenblatt, chairman of the American Names Assn.

For the most part, however, the charges aren't sticking. While the idealistic fraud cop may be guilty of overinflating the names' expectations, his proposed settlement is winning widespread accep-

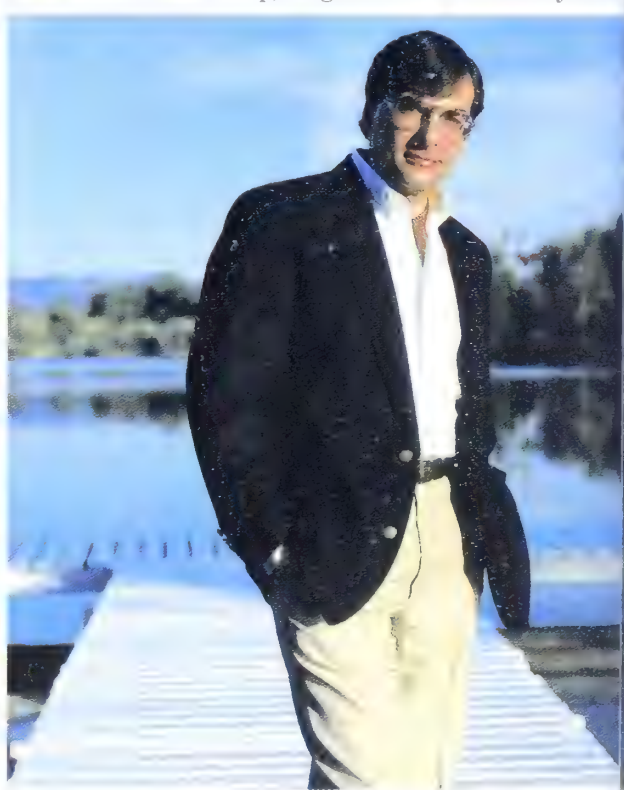
tance. In spite of intense lobbying by the powerful names, whose ranks include Supreme Court Justice Stephen G. Breyer and Charles R. Schwab, regulators from 37 states representing more than 80% of U.S. investors have accepted the deal—enough to make it binding. As a result, the odds of the 308-year-old institution's survival have improved and a possible crisis in the global insurance market has been averted. “There are some types of insurance that Lloyd's provides that aren't available elsewhere,” says Richard Wiebe, California's deputy insurance commissioner. “If the securities regulators hadn't reached a

settlement, it could have been chaotic.” **CHANGE OF HEART.** The accusations of selling out fraud victims have stung Feigin, 47, who has devoted much of his career to prosecuting scam artists. After joining the Colorado securities commission in 1982, Feigin built his reputation by breaking up penny-stock operations—and then led

two state regulator task forces attacking the problem. “If you want to look at somebody with a track record for protecting investors, Phil has the best one of any of us,” says Stephen Diamond, Maine's securities administrator.

Indeed, securities fraud disturbs Feigin so much that he sings about it. An accomplished guitarist who is a devotee of folk artists such as Peter, Paul, and Mary, Feigin has written near “an albumful” of ballads about subjects such as the Orange County bankruptcy and the savings and loan crisis. His ode to Ivan F. Boesky, entitled *Stealing*, sung to the tune of *Feelings*. (“Stealing nothing more than stealing/Inside information; oh, they'll never know.”)

When U.S. names first appealed for help, Feigin concluded that Lloyd's re-



WARY: Feigin feared Lloyd's fall would spread ruin

representatives had behaved as badly as some of the other characters he croaked about. But the more he learned about the case, the more he questioned whether pursuing the state fraud suits made sense. While suing Lloyd's might save American investors some money, it threatened to torpedo the exchange rescue plan, harming thousands of innocent companies and individuals who had purchased policies from Lloyd's. As a state official, he was obligated to take their interests into account, too.

At a critical meeting with state insurance regulators in New York in July, Feigin learned just how devastating the collapse of Lloyd's would be to the entire reinsurance market, perhaps rendering it impossible to obtain some types of high-risk coverage. Because

Despite the barbs, the commissioner's part is winning acceptance with regulators

he state suits hinged on the untested
gal notion that becoming a name was
re purchasing a security, Feigin ques-
ioned whether they would succeed. And
e believed that, with its survival at
ake, Lloyd's would litigate the cases
gressively. Given the budgets of state
ficials and the range of investors they
re obliged to protect, he was certain
any commissioners would rather settle
an risk a "nuclear war" with Lloyd's.
Unaware of Feigin's change of heart,
merican names were shocked to dis-
ver that his deal calls for them to

THE SINGING REGULATOR

Philip A. Feigin
missioner, Colorado Securities Div.

DATE Mar. 7, 1949.

ACTION University of Wisconsin,
71; Pepperdine, JD 1977.

ONAL Married to Barbara Walker,
do's banking commissioner. The
ll themselves 'Nick and Nora
ator.'

Y Folksinging. A one-time per-
at antiwar rallies, Feigin now
allads about securities fraud at
gs of state regulators.

IT ACCOMPLISHMENT Won a
rent that keeps Lloyd's afloat
aving U.S. investors up to \$63

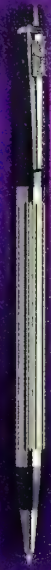
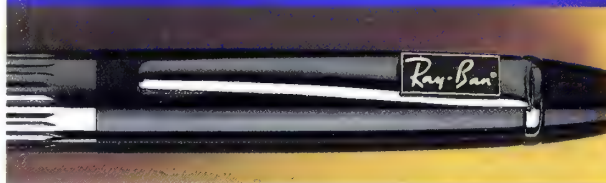
CHALLENGE Defending the set-
t against investors who wanted a
deal.

ay up more than \$200 million to
yrd's—potentially pushing many into
sonal bankruptcy. Now, they're
unting a last-ditch campaign to per-
ude states to back out of the deal. In
embarrassing setback for Feigin in
own backyard, Colorado Attorney
neral (and GOP U.S. Senate hopeful)
le A. Norton says she is considering
attempt to undo the state's accep-
ce of the deal.

Feigin says Norton has no power to
rrule his authorization of the accord.
has lost 14 pounds since taking the
yrd's assignment, and he knows his
d is costing others sleep. "Sometimes
best solution is not the most popular
," he says. That could be the chorus
the whole unhappy ballad.

By Mike France in New York, with
ndra Dallas in Denver and Julia
mn in London

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THE SECRET WORLD

Widely despised, shorts are often seen as unscrupulous rumormongers. A closer look tells a different story

Solv-Ex President and Chief Financial Officer W. Jack Butler is the kind of man who might have been called a captain of industry, back in the days when that really meant something. An erect, dignified man in his late seventies, he spent 35 years with Mobil Oil and served as chairman of Mobil Saudi Arabia in the heady days of the 1970s. Solv-Ex has a process for turning oil-laden sand into crude oil—a vital, almost unimaginably lucrative process, if it succeeds. And to Butler, it's more than that. "I don't just want to make money," he says. "I want to do something for my country."

But Solv-Ex Corp. is under attack. Picking at a salad in a café near his Park Avenue apartment, Butler stoically ticks off the problems. Rumors of improprieties and involvement by penny-stock manipulators. A Securities & Exchange Commission investigation. An incessant drumbeat of negative publicity has slashed the company's share price by 60% over the past few months and has so hurt its reputation that its efforts to finance its sand-into-oil project, up in Alberta, Canada, have been gravely harmed. "We feel we're a good company," he says. "Operating ethically. Good technology." And it would succeed, he insists, if it weren't for a mudslinging campaign by a small band of stock-bashing traders: the short-sellers.

About half a mile downtown, a man about half

Butler's age, polo-shirted and barefoot, is staring at a stock-trading screen that shows some cheerful information: The Dow Jones industrial average is falling. Something resembling panic seems to be taking place, and at trading desks around the country, men and women are picking up their phones and yelling "Sell!" This man is on the phone with his trader, but he's buying—replacing stocks that he had previously borrowed and sold, hoping that their prices would decline. They have. But there is one stock he borrowed and sold that he is not replacing. It is Solv-Ex. For he feels Solv-Ex has a long way to go before it stops falling. The company, he asserts, is burning cash like an overheated furnace—one that will eventually blow up.

Short-sellers. They're as old as Wall Street. And though much has changed there, this has not: No one on the Street is more widely despised. Short-sellers were profiteers in the 1929 crash; aggressive "stock-busters," led by the flamboyant Feshbach brothers, in the 1980s; and, nowadays, secrecy-worshipping, often embattled traders who bet on what is almost



Cover Story

The Truth About Those That Sell Short

The murky world of short-selling is beset by a host of misleading—and sometimes downright false—perceptions. To clear up a few:

DATA BUSINESS WEEK

PERCEPTION

Short-selling makes prices decline.



REALITY

Yes, shorts sometimes seek bad publicity that hurts stocks. But since they can't sell an issue when it's falling, they can't really torpedo stocks.

OF SHORT-SELLERS



un-American—that share prices will collapse. The bull market made them suffer until just the past few weeks. An investor who put \$100,000 in the hands of a typical short-seller at yearend 1990 would have \$50,400 by the middle of this year.

But the misery that has enshrouded the market lately—NASDAQ in particular—has been mother's milk for short-sellers. In recent weeks, they have come roaring back, with shorts gaining 10% in June and another 10% to 15% through mid-July, according to Harry Strunk, a Palm Beach (Fla.) investment consultant who tracks short-sellers (chart, page 66). The short-seller revival is likely to exacerbate their reputation as piranhas—particularly among investors in small-cap stocks, who often view short-sellers as the assassins of Corporate America. "Small companies can be seriously affected by short-sellers. Some of these shorts target particular issuers and don't know a damn thing about the companies they're shorting," says Edward Mishkin, a prominent New York securities lawyer and a vocal critic of short-sellers.

BET OR PUSH? Even among hardened pros on Wall Street, particularly institutional investors, small-stock underwriters, and brokerage analysts, shorts are shunned and hated. "Fund managers will tell you: 'I don't want anyone shorting my stock.' They don't want anyone making money on their mistakes," says one Wall Street executive who routinely deals with both shorts and "longs"—conventional investors. The detractors of short-sellers maintain that shorts don't just bet on share-price declines, they make them happen. Shorts are blamed for the travails of dozens of high-flying stocks that have taken heavy hits during the recent NASDAQ massacre: Solv-Ex, Diana, WellCare Management, Presstek, SyQuest Technology, and a host of other high-tech companies. "Short-selling and bear raids are part of the business," concedes Solv-Ex CEO John S. Rendall. "But when you put out false rumors and get the SEC involved—that, I believe, is criminal activity."

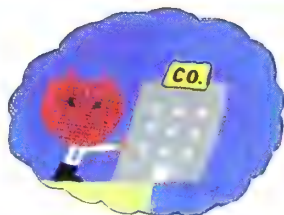
Are shorts the bane of Wall Street? Are they villains or scapegoats, responsible whistle-blowers or venal rumormong-

PERCEPTION

Short-sellers are a destructive force in markets.

REALITY

Shorts add to liquidity in markets—selling and buying when buying and selling are rising and falling most—during market declines. Shorts are accounting irregularities and mismanagement. They also counteract the damage from companies that are in shaky financial health and thus are unwise investments.



PERCEPTION

Voracious short-sellers destroy companies by cutting off their access to capital.

REALITY

Companies targeted by shorts are often in shaky financial health and thus are unwise investments.

PERCEPTION

"Naked" short-selling—selling stocks that haven't been borrowed—is rife in the markets and helps drive share prices down.

REALITY

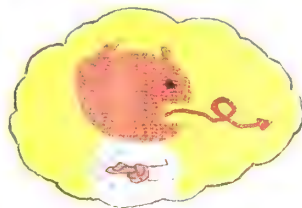
Naked shorting takes place, but its prevalence has been exaggerated by critics. Market makers can "go naked" in the normal course of business, but they risk heavy penalties if they do so to bet that a stock will fall.

PERCEPTION

Short-sellers spread lies about companies.

REALITY

Sometimes. But more often than not, their research is among the most detailed and accurate in the investing community.



Because of their contrarian stance and the liquidity they provide, shorts have an overwhelmingly positive impact

gers? To find the answer, BUSINESS WEEK delved into the world of the short-sellers. It wasn't always easy, for shorts cherish their privacy, and many fear attention with an intensity that can border on paranoia. The picture that emerged is dramatically at odds with the conventional view of short-sellers as hood-like market-manipulators.

To begin with, only a tiny fraction of short sales are bets on the direction of stocks. The vast majority—perhaps 98% by one informed estimate—are merely efforts to hedge stock holdings or take advantage of arbitrage opportunities with other forms of investment. Traders who exclusively short-sell are but a tiny cadre of market players—a handful of partnerships and small brokerage firms. Despite their raptor-like image, they are often victims—not perpetrators—of stock manipulation. And though they can certainly put a dent in stocks by leaking stories to the media, the image of “stock-busters” who can drive down share prices is overblown. Exchange and NASDAQ rules ban short sales while a stock is

declining. This “uptick rule,” which allows shorting only when the most recent price

Cover Story

change was positive, makes it tough to beat down stocks by short-selling alone.

To be sure, there are instances of questionable practices by shorts, such as the aggressive short-selling that allegedly led to the demise of the Adler Coleman & Co. penny-stock trade-clearing firm last year. Regulators are investigating charges by Mishkin, the court-appointed trustee, that shorts engaged in such nefarious practices as “naked” short-selling—shorting stocks that haven't been borrowed. Federal authorities are investigating the short-selling of Organogenesis Inc., a biotechnology company, because of allegations that false information was spread about the company (BW—Apr. 22). But the overwhelmingly negative publicity overshadows the contributions shorts make to the market—particularly in raging bull markets, when Wall Street hype runs rampant.

Because of their contrarian stance and the liquidity they bring to bear, short-sellers have an overwhelmingly positive impact on the market. They are often the market's first line of defense against financial fraud—frequently alerting regulators to scams and accounting irregularities, as was the case with now defunct zzzz-Best and College Boun. And short-selling abuses have often been exaggerated. Naked short-selling certainly happens, but vastly more commonplace is the “short squeeze,” a chain of events that can be a blatant effort to punish short-sellers by forcing them to buy stocks when they are artificially high (illustration below).

REALITY CHECK. The market's hostility toward short-sellers makes shorting a risky strategy often best left to professionals. Still, everyday investors have a great deal to learn from short-sellers. Even when they are wrong or their timing is off, short-sellers offer a refreshing reality check on the overvarnished bullishness so prevalent on Wall Street. Short-sellers include some of the most talented analysts in the investment arena and are noted for their adroit, labor-intensive research. One short-selling partnership even includes among its analysts a retired physician to evaluate biotechnology stocks. But at bottom, what gives shorts an edge is sheer shoe leather.

“Shoe leather” might well be Manuel Asensio's middle name. Like most short-sellers nowadays, Asensio has his fingers in other pies—from conventional money management to municipal-bond underwriting. But short-selling is clearly his first love. Asensio, who runs Asensio & Co., a New York investment boutique, is a rarity among short-sellers, for he is anything but secretive. For the first time since the 1980s, when the flamboyant Feshbach brothers of Palo Alto, Cal., made some highly publicized stock pans, shorts have a self-appointed... well, “point man” might be the word. “I respect what he does,” says one short who has never met Asensio but has read his research and respects the guts shown by his public stance on stocks. “He is totally associated with his

Four Ways Shorts Get Stung

There are four distinct types of short squeezes. All force short-sellers to buy back stock, thereby driving up share prices.

DATA: BUSINESS WEEK

THE TRADE

A short-seller sells shares that are borrowed, either from an institutional investor or—more perilously—from a retail brokerage. Shares in any margin account can be borrowed if they haven't been fully paid for. The short hopes to eventually replace the borrowed stock at a lower price, pocketing the difference.

THE MARKET-FORCES SQUEEZE

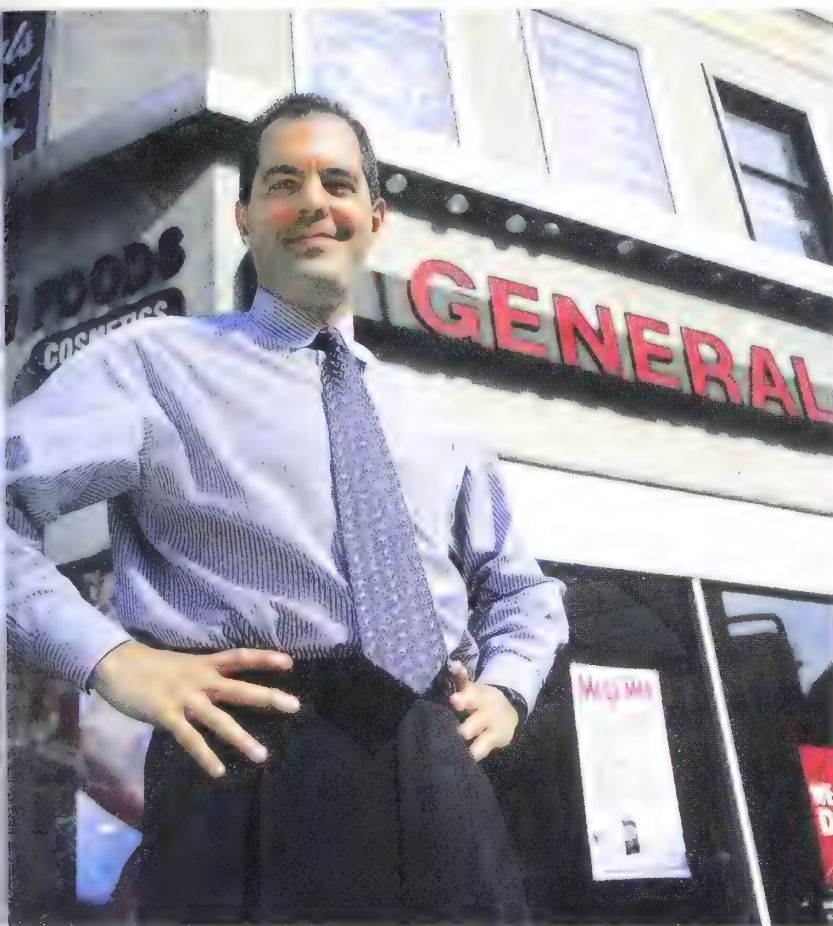
In the most typical short squeeze, market forces or favorable news drive up share prices. If prices move up sharply, shorts must immediately put up more collateral—or return the shares.



THE INSTITUTIONAL SQUEEZE

Institutional shareholders—mutual funds and pension funds—who loan out shares to short-sellers can demand their return at any time. When that happens, the shorts must hand them over.





clients. It's a small operation—just three analysts aside from Asensio, all squeezed into a cramped suite of offices in midtown Manhattan. "I never subordinate my own judgment or fact-finding," says Asensio. Not surprisingly, he routinely puts in 14-hour days and hasn't taken a vacation since February—of 1993.

DETAILS, DETAILS. Although his embrace of the limelight sets him apart from most shorts—he even issues press releases announcing his short picks—as an analyst, Asensio hews strictly to the exhaustive, detail-oriented approach that is the short-sellers' stock in trade. A good example is his short sale of General Nutrition Cos. shares last January. Red flags were fluttering: a high price-earnings ratio, selling by corporate insiders, and oversaturation of the health-food market. "I saw nothing but bad news in the future. There were problems with the vitamin market, insiders were bailing out, same-store sales were weak. What more can you need?"

OPEN HAND

Like his peers, Asensio does exhaustive research—but he's far from secretive

Asensio recalls.

There was more. Asensio got wind of an upcoming study on the benefits of "antioxidants" such as beta carotene—a nutritional supplement that is widely promoted at

s—his short picks—"and that is something you don't see of nowadays." At least, not among short-sellers.

A native of Cuba who came to the U.S. with his family in '62, the 41-year-old Asensio began trading while he was a student at Harvard University in the early 1980s. After working as a venture-capital dealmaker and an investment banker at Bear Stearns & Co., he went into business for himself. Asensio manages about \$100 million, mostly for wealthy

GNC stores. He began by calling secretaries and receptionists at hospitals where the study had been taking place. "I got a flavor of what was going on, a smell," Asensio recalls. He liked the odor. On the day of the release of the study, which cast doubt on the efficacy of beta-carotene supplements, Asensio hired a lawyer to get hold of it the instant it was available in Washington. Not a messenger service? "No way. I use the A-Team," says Asensio.

Asensio shorted the stock—and issued a press release dumping on the company. Nothing happened. "Their defense was that beta carotene was only a small percentage of their sales," says Asensio. "But I said at the time: 'The problem is store traffic, stupid!' People come into the stores for antioxidants." Eventually, GNC announced that same-store sales were on the wane, and the shares fell. GNC stock, which traded at 23 in early January, is now at 14. (A spokesman declined to comment on Asensio but says GNC "firmly believes our business strategy is in place and working.")

Nowadays, Asensio's No. 1 stock is a company that he despises—and the feeling is mutual. It is Diana Corp., a Milwaukee company that is in the process of dramatically shifting its product line from meat distribution to telecommunications equipment. Asensio thinks Diana is an ill-managed company that has put out misleading information; Diana says Asensio has been doing the same thing. "He has continually made misstatements about our

ACCOUNT SWITCH

Shareholders move from margin to cash accounts, must return shares borrowed from margin account.



THE HYPE SQUEEZE



Common among thinly traded shares. The company, or stock promoters, intentionally pressure shorts by praising the stock

and investors or issuing overoptimistic press releases to drive up the share price.

THE BUY-IN

When shorts must return borrowed stock, the shares must be bought on the open market. Thus, short-sellers can sustain huge losses if prices have risen—and since their purchases drive up prices still further, they boost the pain of fellow short-sellers.

company," fumes Diana Chief Executive Richard Y. Fisher.

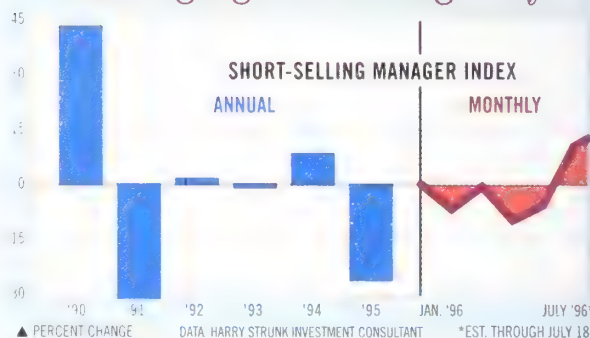
Asensio has shared his views with the message boards of America Online Inc., where they are welcomed. But Wall Street is another matter. Asensio and other shorts complain that brokerage analysts and fund managers have a uniformly hostile attitude and are loath to even return their calls. "I would love for someone to call me and tell me that a stock that I own is a piece of s—," says Asensio. "But I'll talk to some pension-fund manager who owns \$4 million of some stock, which he bought with employee money. I'll tell him something is wrong with the company—and he gets emotional! It is ridiculous. It is irresponsible." Another short says he attempted to bring accounting irregularities to the attention of a company's auditors and found that his calls were not returned. "I wound up faxing them," says the short. The accounting allegations were eventually acknowledged and corrected by the company.

The whistle-blowing element of short-selling is a sensitive subject. Short-sellers don't like to trumpet it, but if they feel that a company is using improper accounting or not making adequate public disclosures, they have no qualms about contacting the companies' auditors, the exchanges, the SEC, and lawyers seek-

ing to bring class actions on behalf of disgruntled investors. And then there's the financial press. "I like talking to the press. We're like investigative reporters ourselves," says one short. Another short-seller keeps a small stack of articles from financial publications in which he was a source—all exposing fraudulent and shady companies that ripped off thousands of shareholders. Indeed, many prominent financial frauds of recent years were targeted by short-sellers long before they were picked up by regulators and the press. Shorts exposed the troubles besetting WellCare Management Group Inc. and Future Healthcare Inc. in recent months.

Cover Story

Emerging From Purgatory



The saga of WellCare, a Kingston (N.Y.) HMO, epitomizes the role shorts play as whistle-blowers. "We talked to doctors who worked for the company," one short recalls. When word of possible accounting improprieties surfaced last March, the company pointed the finger at "untruths circulating as rumors" coinciding with a "buildup of a substantial short position in WellCare's stock."

For a while, the company hanged tough, hiring a private investigative firm, Kroll Associates Inc., to look into the blemishing of the company. But the shorts were on the right track. Two months later, WellCare restated its previously reported 1995 earnings—slashing them by 80%. A spokesman admits that "some of the issues [short-sellers] raised had some accuracy" but that others were "overstated."

WellCare was a smashing victory for the shorts, as was SyQuest Technology Inc., a disk-drive maker that has attracted shorts because of its propensity to consume cash—often a tip-off of financial woes. The shares have fallen to 6 from a takeover-fed high of \$17 in May. (SyQuest won't comment on the shorting of its stock.) Aggressive account-

THE 'BAD BOYS' OF CHICAGO ARBITRAGE

When Chicago Stock Exchange officials showed up at the trading firm Scattered Corp. for a routine audit two years ago, principal Leon A. Greenblatt was ready. He answered the door with a toy dart gun sticking out of his pocket, a pool cue in his hand, and a shot of Jack Daniels splashed on his face. Ushering his guests into a room without a table, he handed over the firm's records 10 pages at a time. These days, the auditors ask Greenblatt to send his books across the street to their offices.

No, the Chicago Stock Exchange doesn't like Leon Greenblatt—and it's not just because of his, well, unconventional personal style. Three years ago, at age 33, Greenblatt did

something that brought down upon him the kind of regulatory wrath—a \$6 million fine—that is usually reserved for insider traders and penny-stock peddlers. Greenblatt provoked the Chicago exchange's ire during an audacious arbitrage play on the shares of bankrupt steelmaker LTV Corp. Greenblatt sold more LTV stock than actually existed,

replacing it with cheap warrants—and reaping a \$27 million profit in 22 trading days. So far, he has gotten away with it—and won a little-noted legal victory in the ongoing war between longs and shorts.

Scattered principals Greenblatt, Andrew J. Helka, and Richard O. Nichols may be "reckless gamblers, sharpies, wise guys, exploiters of loopholes, even violators of the letter or

A judge said the partners may be "gamblers" and "sharpies," yet he upheld their LTV victory

spirit of the rules," wrote Appellate Judge Richard A. Posner, one of the federal judiciary's leading economic thinkers, in a February, 1995, ruling. Posner noted that Scattered's trading in LTV helped bring together the price of the stock and its underlying value, thereby playing a valuable role in the marketplace. Thus, the firm furthered—not violated—the objectives of securities law, the judge concluded, upholding a Scattered victory in a lawsuit brought by injured LTV investors in a lower court. \$6 million fine the Chicago exchange levied on Scattered is on hold pending appeal.



d stock sales by corporate officers are other red flags. Recently, shorts have zeroed in on Lone Star Steakhouse & Saloon and Landry's Seafood Restaurants, as well as two manufacturers of sunglasses—Oakley and Sunglass Hut Trading—because of high insider selling. Sunglass Hut Corp. CEO Mark B. Chadsey says his recent stock sale still leaves him with a large stake in the company and does not reflect any lack of confidence in the company.

PARTIAL OVERSIGHT? Specialized expertise is another area where shorts can bring powerful resources to bear. One short-seller, who has a physician on staff, is shorting Oxigene Inc., a New York pharmaceutical company. The physician-analyst studied a company-sponsored clinical study of its flagship product, an anticancer medication, and found it offered no evidence that the product is effective. As is often the case, however, the company has a dramatically different point of view. Ronald Pero, Oxigene's chief scientific officer, says the results are dead wrong and that the study offers evidence of the drug's efficacy.

Right or wrong, research like this is often shared among short-sellers, which gives rise to the not unjustified view that there are "rings" of short-sellers. Actually, "rings" may be a bit pejorative, since institutional investors—and brokerages, of course—are similarly ready to share stock picks. But there's a darker side to short-selling that has recently gained attention in the wake of the failure last year of Hanover Sterling, a money-stock broker, and the subsequent failure of Adler Coleman, the clearing firm that executed Hanover's trades. Trustee Mishkin found that Hanover and Adler were driven out of business by short-sellers. The shorts, in response, accuse Mishkin of enacting a short squeeze that deliberately gave them losses. The two sides are slugging it out in court.

Mishkin maintains that what happened to Adler Coleman is the tip of the iceberg. He recently stated in court documents that one of the shorts allegedly involved in the Adler Coleman failure, Fiero Brothers, went on to target Solv-Ex.

Many financial frauds of late were targeted by shorts well before regulators spotted them

That is denied by John Fiero, the head of the firm, who notes that he has both bought and sold short Solv-Ex shares. "I'm a trader, not a short-seller," says Fiero.

If the bankruptcy court determines that Adler Coleman was driven out of business by the shorts, it would be a rare legal victory for the "longs." In one landmark case involving short-selling by Scattered Corp., a Chicago stock-trading

firm, Scattered won a ringing victory (box). Moreover, shorts are often the victims of manipulation in short squeezes. Squeezes have become commonplace in recent months and have only abated during the recent market setback.

A squeeze can be quite benign—perhaps a bull market putting pressure on short-sellers. But it can also be a deliberate effort to put shorts under pressure and push up prices by forcing shorts to buy back their shares. To bet on a share-price decline, short-sellers must sell stocks that they borrow. There are two sources of stock loans: institutions and brokerage accounts. Institutions lend shares for a small fee—usually just one-quarter of 1% of the value of the shares. Brokers are permitted to lend shares from their own accounts and from customers' margin accounts that have not been fully paid for.

But shares available for short-selling are growing increasingly scarce—particularly for the NASDAQ issues that are most popular with short-sellers. One brokerage executive, who requested anonymity, notes that institutions are increasingly chary about lending shares to shorts. The result is that shorts must borrow stock from retail brokerages, leaving



TRICK SHOTS Greenblatt (left) and Nichols cover all the angles

bankruptcy arbitrage. "He plays it fast and loose, and the people who are the most pissed off are the old-timers who don't understand the game," says one exchange member.

Greenblatt makes a fetish of secrecy, providing only sketchy details of his arbitrage strategies. In a typical trade, Scattered sells the stock of a company about to emerge from bankruptcy while buying newly issued shares or warrants that replace the old stock. If the old stock trades at a higher price than the new issue, Scattered can make money.

In LTV, Scattered found a huge anomaly: The company had announced a plan of reorganization under which its existing stock would be replaced by new stock. Stockholders received warrants

suers involved.

Sentiment still runs hot against the likes of Scattered—and no wonder. Greenblatt flaunts a bad-boy image even as he continues to profit from

entitling them to purchase some of the new stock at a price of about 3.2¢ per share. Even after the plan was confirmed, the old stock traded at an average of 18¢. Since the warrants greatly outnumbered the existing shares, Scattered kept selling stock and buying warrants until it had sold 180 million shares—58 million more than existed.

BLIND BANDWAGON. Speculators apparently were betting that the stock would rise just before its terminal plunge. Others simply didn't understand or investigate the planned fate of the old shares. Certainly, the facts were no secret: LTV repeatedly warned that its stock price was unsustainable.

Greenblatt relies on a creative interpretation of the rules. He claims, for instance, that as a market maker performing arbitrage, his firm is exempt from the rule requiring short-sellers to settle up within several days. Asked how he finds his deals, Greenblatt merely smiles. He warns off those who might seek to imitate his strategies: "You have to have the proper experience. If you don't, you get wiped out." An all too familiar experience for short-sellers in recent years.

By Greg Burns in Chicago

The U.S. Supreme Court on June 19, 1995, let stand the Posner ruling. The Chicago Stock Exchange declined comment on Scattered or the legal is-

There are certainly cases of excess. Just ask Organogenesis or Adler Coleman's bankruptcy trustee

themselves open to short squeezes involving customers demanding delivery of their certificates.

A vivid—and unusually blatant—example of a short squeeze took place with Solv-Ex. On Feb. 5, after the stock fell 30% in a matter of days, the company faxed to brokers and shareholders a "Notice to Shareholders." "To help you control the value of your investment on a steady basis," the notice read, "we suggest that you request delivery of the Solv-Ex certificates from your broker as soon as possible."

It worked. Solv-Ex shares began climbing again, approaching the old highs by Feb. 21. "I was bought in at around that time," one short-seller recalls ruefully. Says a stock-loan official at a major brokerage firm: "Very few short-sellers know the mechanics of short-selling. What they don't understand is that when a stock is not available from institutional sources and comes from the Street, they can get squeezed." The risks are magnified, he says, if the source of the stock loan is a brokerage that makes a practice of squeezing shorts.

LOOPHOLES. Short squeezes are not a problem for one of the most lucrative, little-noted, and troublesome forms of short-selling—shorting of private-issue stock sold abroad under Regulation S of the securities laws. According to short-sellers and regulators, who are looking into beefed-up regulation of Regulation S stock, such short sales are carried out by favored foreign investors—or sometimes, illegally, by corporate insiders. No matter who carries them out, however, the deals are invariably extremely lucrative.

When used to raise capital for small companies, Regulation S stock is usually sold at a discount to the prevailing market price. The stock may not be sold in the U.S. for at least 40 days. The existence of such offerings is often considered a red flag by shorts because of the dilutive effect of the stock when it is eventually sold in the U.S.—and because they show that the company may be having trouble raising capital. Shorts insist that insiders sometimes buy such cut-rate stock through foreign shell corporations and then sell short in the U.S. market—locking in the profit between the discounted shares and the shares sold in the U.S. The SEC last year acknowledged abuses in Regulation S offerings, including improper short sales, and is considering tightening the rules.

But any rule changes are unlikely to curb foreign investors, who often sell short—quite legally—to lock in their

profits. Solv-Ex, which has made heavy use of offshore offerings, recently disclosed that the Curacao-based GFL Advantage Fund bought 530,000 cut-rate shares in a Regulation S offering and then sold short in the U.S. a half-million shares—one-quarter of Solv-Ex' short interest—locking in a profit that probably exceeded \$2 a share, or \$1 million. (The filing says the short sale was conducted "to hedge GFL's downside market exposure at the time.") GFL was still short as of early July—in the midst of Solv-Ex' campaign against the shorts.

FOREIGN PRESSURE. The offshore shares have been registered for sale in the U.S., where they will further dilute the equity of Solv-Ex' hard-pressed shareholders. So Solv-Ex executives seem to be right. Short-selling is hurting shareholders—though the problem is from Solv-Ex' overseas friends and not from home-grown short-sellers.

But what about the other shorts in Solv-Ex—the ones who are betting that it's a fair balloon? Are they right? Is the company correct in its view that shorts are a roadblock on the path to oil-patch immortality? Ultimately, the markets—both the oil and stock markets—will answer that question. But so far, the outlook for Solv-Ex is not so good, because the shorts are playing hardball. Somehow, a short-seller obtained a company-sponsored engineering report and had them evaluated by an engineering firm of his own. The short-seller's study contends that the Solv-Ex process is "particularly unique, nor does it appear to be capable of being effectively protected by defensive comprehensive patents, nor is it particularly different

from competing oil-extraction methods. The evaluation goes on to estimate that the project, at full capacity, will yield a \$10.5 million annual loss, vs. the \$24.7 million profit projected by the company. CEO Rendall strongly disputes the study and has commissioned Kroll Associates, the private investigative firm that worked for WellCare to probe the short-sellers' activities.

That's the way it is in the world of short-selling: charge and countercharge, study vs. study. The shorts can be nasty at times. But their excesses are like a drop of ink in the ocean—an ocean of Wall Street hype. For the first time in this bull market, short-sellers are finally beginning to see the playing field tip, just as in their favor. They are unlikely to wind up winners if the bull market picks up speed again. Nor will they pick up any friends. In their ceaseless, profit-driven quest for rotten apples, short-sellers will continue in their role as the market's hated—but indispensable—prophets of doom.

By Gary Weiss in New York

Cover Story



UNDER ATTACK
Solv-Ex CEO
Rendall hired
Kroll Associates
to investigate
short-sellers'
activities

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INSURANCE

CAN ART RYAN MOVE 'THE ROCK'?

As legal woes persist, he's slowly revitalizing Prudential

When Arthur F. Ryan arrived at Prudential Insurance Co. at the end of 1994, the new chairman and chief executive found a company in something of a shambles. "The Rock" had just admitted its securities unit had sold limited partnerships fraudulently, which ultimately cost it \$1.5 billion. Evidence was mounting of improper sales practices in its individual life insurance unit that by April had evolved into a multistate regulatory probe. Lawsuits were starting to proliferate. And its once-pristine reputation was badly tarnished. More broadly, Ryan faced a huge, unwieldy institution that was badly adrift. Its strategy was floundering, technology systems were outmoded, costs were bloated, market share was under pressure, and its financials were anemic.

A year and a half later, Ryan seems

to be taking all the right steps to revitalize the nation's largest insurer. He has been working with regulators to resolve the life-insurance sales scandal. On July 9, Pru agreed to a multistate settlement plan with a \$35 million fine, the biggest penalty ever levied on an insurer, and restitution for abused policyholders that could cost more than \$1 billion. The next day, Ryan took out full-page newspaper ads to apologize for the "intolerable," deceptive sales practices. He has revamped the sales system, fired hundreds of agents and managers suspected of wrongdoing, and bolstered internal controls.

Ryan has also put in place a strategy to improve Pru's tepid performance. He has streamlined management, shed more than \$1.4 billion worth of nonstrategic businesses, and instituted an \$800 million annual cost-savings program. With

PRU CARE: *Ryan's biggest challenge will be to change the firm's culture*

almost \$12 billion in capital at midyear, Prudential is positioned to absorb not only the cost of paying off policyholders for past sins but also is better able to stem a dip in its debt ratings and invest in the future. "I believe that a very large portion of the work to fix [the company] has been accomplished," says Ryan. "We are now able to focus more on how we are going to build."

WEAK FINANCIALS. Ryan's repair job won't be easy. His biggest challenge will be to fundamentally change the firm's culture. "This has been a company where the CEO could make a decision and some guy four layers down could derail it," says one Prudential insider.

The company's financials are still lagging. It earned a mediocre \$579 million in 1995; Ryan is targeting a somewhat better \$600 to \$700 million this year. Still, "this organization should be earning in the range of \$1.5 billion a year," says David A. Havens, Standard & Poor's director of insurance rating services. Pru is still underperforming other mutual insurers, says Lawrence G. Mayewski, an A.M. Best Co. senior vice-president. Using Ryan's 1996 earnings goal, Prudential's return on capital plus or capital would be about 7%. That's up from 6.5% in 1995 but well below the 9.0% to 9.25% Mayewski expects for the industry in 1996. Mayew-

though, says Ryan has lifted Prudential's risk-based capital ratio—a measure of its insolvency cushion—which grew from 171% at the end of 1994, below the industry average, to an above average 235% at the end of 1995.

Ryan also must reverse some significant losses in market share. Take asset management. The giant has slipped fifth place in assets in 1995, from second place just the year before, according to an *Institutional Investor* survey. And despite some paring, the Rock still is perceived as a mishmash of businesses—life insurance, property and casualty insurance, health care, securities brokerage, banking, as well as asset management. “Pru’s in too many businesses. Art’s gotten them out of some of the peripheral stuff, but in today’s world, they have really got to focus more on what they have,” says Richard L. Huber, vice-chairman at competitor Aetna Life & Casualty Co.

By all accounts, Ryan’s background would seem to equip him for the job. The Chase Manhattan veteran is no stranger to adversity. In 1990, Ryan was appointed president with a mandate to join new Chairman and CEO Thomas G. Labrecque in dealing with the bank’s mammoth loan losses. They shed costs and focused Chase on its longest businesses. Ryan became known as “the gorilla” for his tough management style. When he left, in the words of a Chase banker, the bank had “a lot to walk down the aisle with” in the 1995 sale to Chemical Banking Corp.

BLACK STUDY. Brooklyn-born Ryan, 53, a self-described “erratic” golfer. But a former chain smoker brings a different approach to his new job. “He’s very down to earth. There is no hidden political agenda,” says Anthony P. Terracino, a former Chase colleague and now president of First Union Corp. “He has a very informal style,” says Chase alumnus Huber. “But at the end of the day, he will deliver or you are history. That’s

unusual in any component of the insurance industry.” Adds Prudential board member and former Merck & Co. CEO P. Roy Vagelos: “He’s not blown over by tough problems.” Fellow director and Princeton University professor Burton G. Malkiel calls Ryan “a fast study...who is very willing to make sweeping changes.”

Among Ryan’s most important initiatives is to build Pru’s share of aging baby-boomers’ savings. He hired Rodger A. Lawson, considered the architect of Fidelity Investment Co.’s successful marketing strategy of the 1980s, to lead Pru’s marketing effort. Ryan also formed a new money management group with \$200 billion in assets under management to consolidate mutual funds, individual annuities, guaranteed investment contracts, 401(k)s, and pension plans. Unit head E. Michael Caulfield, a respected Prudential veteran, says the group has a shot at being “the growth engine of the organization.”

Ryan will keep Prudential Securities Inc. as a key part of his plan to accumulate savings assets despite Street gossip that the unit is for sale. “Art sees us as his distributor to higher net-worth individuals,” says Hardwick Simmons, the CEO of Prudential Securities.

The CEO’s efforts seem to be bearing fruit. In the first quarter, Prudential is off to a good start, with profits of \$441 million. Ryan says projected 1996 profits of \$600 million to \$700 million should pass \$1.1 billion in either 1997 or 1998. That includes an estimated 1996 restructuring

charge of at least \$800 million for cost cuts. But these projections do not include life-insurance restitution costs.

Prudential has made progress toward resolving its legal woes, but the job is not over. If the multistate settlement is accepted by policyholders and lawyers, who are currently insisting on major changes, the odds are the plan would largely resolve Pru’s fraudulent sales practice allegations. Thirty-seven

states plus the District of Columbia have agreed to let the plan be offered in their states. But 240 sales-practice related lawsuits, including 22 as yet uncertified class actions. There are another 21 suits by alleged whistle-blowers still in the works. Some of these could be potential land mines. In an arbitration case now before the National Association of Securities Dealers, two former Prudential Insurance managers charge they brought sales abuses to Ryan’s attention but that their complaints were ignored, supporting documents destroyed, and

that they were fired in retaliation. The company says the managers were dismissed for failure to supervise and says it expects to be fully vindicated.

Prudential director and former Federal Reserve Board Chairman Paul A. Volcker minimizes the outstanding liabilities. “Prudential has been under very close scrutiny,” he says. “We are at the bottom of the problems, whatever happens to the legal suits.”

Ultimately, Ryan will be judged on his ability to create an effective strategy. His plans, while more focused, are not unique. Every bank, securities company, and insurer wants to get its hands on baby boomers’ wallets. Prudential has yet to capitalize on its

strengths: a strong brand name, an enviable distribution system with 20,000 insurance agents and financial planners, 6,000 securities brokers, and millions of customers. As Volcker puts it, “He’s got to move ahead now.”

By Alison Rea, with Leah Nathans Spiro, in New York

Ryan's repair job won't be easy. He must reverse losses in market share and stimulate asset growth. But he expects earnings to pass \$1 billion by 1997 or 1998

ART RYAN IS PUSHING THROUGH REFORMS AT PRU...

...BUT FINANCIALS ARE STILL SO-SO

- ▶ Initiated program to save \$800 million annually
- ▶ Brought in new life-insurance management and revamped sales practices
- ▶ Streamlined corporate structure by reducing operating units
- ▶ Created new money-management operation
- ▶ Raised capital through a reinsurance IPO, sale of mortgage unit, and Canadian insurance operation
- ▶ Reduced company's risk profile

YEAR	PROFIT/LOSS	REVENUE	CAPITAL
1991	2.28	45.74	9.74
1992	0.35	45.32	9.82
1993	0.88	45.97	10.69
1994	-1.18	43.56	9.48
1995	0.58	42.91	11.37

DATA: BUSINESS WEEK, PRUDENTIAL INSURANCE CO. OF AMERICA

By Greg Burns

CIRCUIT BREAKERS DO MORE HARM THAN GOOD

When you're cruising down a busy highway, finding stop signs in your path can be downright dangerous. At the least, they back up traffic, and at worst, cause accidents. In essence, that's the problem with so-called circuit breakers. In the years after the 1987 crash, the New York Stock Exchange and the Chicago Mercantile Exchange imposed rules that halt or slow trading when prices decline a specified amount from the previous day's close. The idea is to prevent stocks from falling too far too fast.

Unfortunately, circuit breakers do more harm than good. By design, the rules "shut down the markets and stop business from being done," says University of Chicago economist Merton H. Miller, a Nobel laureate and board member of the Chicago Merc who opposes these rules. Circuit breakers that impede index-arbitrage trading, which have been triggered frequently in recent months, can increase volatility. Other circuit breakers at the New York Stock Exchange that could close down the entire stock market have never been invoked. But such a closing could be chaotic: A huge traffic jam of sell orders and mass confusion, even panic, when the Big Board tries to reopen trading. Says Miller: "If these things are hit, it's a problem."

PART PUBLIC RELATIONS. At first glance, circuit breakers seem to make sense. After the Dow Jones industrial average plunged 508 points on Oct. 19, 1987, exchanges worried that another precipitous free fall would so spook investors that many might flee the market for good. The new rules were partly public relations. But officials also reasoned that closing or slowing trading would give shell-shocked investors time to cool off, reassess their positions, and most likely start bargain hunting.

Unfortunately, the rules haven't kept pace with the bull market. While the Dow has tripled since

1987, the triggers on circuit breakers have remained unchanged. Now, they're set to go off at even slight provocation: Index-arbitrage trading can be impeded by insignificant moves of 50 points on the Dow, representing less than 1% of its value as of July 24. So far this year, the New York Stock Exchange has invoked that so-called collar more than 70 times vs. 28 for all of 1995. Many investors probably believe that's good, since computerized arbitrage took much of the blame for the '87 crash. But it has never been proven that arbs hurt the market. In fact, arbitrage can reduce volatility by narrowing price discrepancies between the futures and the cash markets.

Not only that; there's little evidence that these circuit breakers work. Some traders, to be sure, point to the volatile trading of July 16, saying the rules saved the day by averting a panicky sell-off of equities. And it's true that a rebound in stock prices coincided with a trading halt in the Chicago Merc stock-index pits. Because the futures shut down as the Dow was plunging, the theory goes, traders had time to regain their nerve.

**In market
downdrafts, it has
been bargain
hunters, not
circuit breakers,
that saved the day**

Yet on several previous occasions when contract limits were triggered, stocks have continued lower. Four times this year, the 12-point limit on futures contracts based on the Standard & Poor's 500-stock index (equivalent to about 100 Dow points) has done nothing to arrest a steep decline in stock prices. And on Mar. 8, the market blew through the same 20-point limit that supposedly worked such magic on July 16. In every case, it was bargain hunters, not circuit breakers, that saved the day. The

stock market found its level when buyers met sellers—which only happens if trading is under way.

The impact of the rules aimed at arbitrage pale beside the New York Stock Exchange circuit breakers. A move of 250 points on the Dow—less than 5%—would shut down trading of stocks altogether, raising the specter of severe disruption and uncertainty. That almost happened on Mar. 8, a Friday, when the Dow plunged 218 points late in the afternoon. Another 32 points would have stranded investors in losing positions over a weekend, certainly undermining public confidence in the marketplace. Fortunately, the market snapped back ahead of the price limit, rallying 46 points just before the close of trading on Friday and setting up a 110-point recovery on the following Monday.

Admitting that some of the rules were obsolete, securities regulators on July 19 came up with a half-hearted compromise. They reduced the time that markets would remain closed once the limits are hit—from one hour to 30 minutes for a 250-point drop. But they also added more limits and left the existing trigger points in place.

A reasonable argument can be made for a very high trigger point at the Big Board in the event of another historic stock-market crash. But the best move is to do away with circuit breakers altogether. "You want the price to fall, because that will bring buyers out of the woodwork," says Miller. Truth is, the public doesn't need the placebo. Small investors were tempered during the 1987 crash of the stock market. Those investors who sold in a panic are unlikely to repeat the same mistake. Investors have wised up. Regulators should do the same.

Burns follows the markets from BUSINESS WEEK's Chicago bureau.



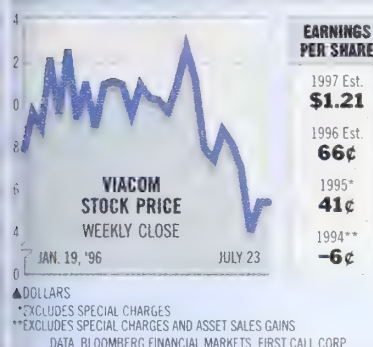
BY GENE G. MARCIAL

WILL VIACOM BE BOFFO AGAIN?

What a difference a year makes. Last summer, media giant Viacom (VIA) was basking in the glory of 1994 acquisitions: Paramount Communications and Blockbuster Entertainment. Viacom shares surged to 54 in September—then slumped to 29 on July 1. A week later, they had edged up to 31. Is Viacom in for more spills?

Don't bet on it, insist money managers who have snapped up Viacom stock. "It has come to ridiculously

SUMMER SLUMP



cheap levels, [but] we're confident management is intent in enhancing shareholder value," says one hedge-fund manager. He thinks the company will continue to sell assets and cut debt.

One move they expect it to make: selling its 12 radio stations, worth \$800 million to \$1 billion. Viacom also owns and operates 12 TV stations. Radio and TV outfits make up 9% of cash flow.

"My guess is that Viacom will take advantage of the premium being paid for radio stations," says Dennis McAlpine, an analyst at Josephthal Lyon & Ross. Viacom's stations are in very profitable markets, he notes. Selling radio stations will bring in cash to reduce Viacom's debt.

Alan Gould, an Oppenheimer analyst, also says Viacom may be thinking of selling radio stations. "But Viacom wouldn't consider any deal unless it is for at least \$1 billion," he figures.

"Viacom is the most attractive stock to follow in media and entertainment," says Gould. "It has the highest growth rate among major studios." Based on projected 1996 earnings, he reckons the stock should be selling at 50.

One Viacom asset that investors underestimate, he says, is Blockbuster, which should generate 30% of Viacom's cash flow this year. Gould thinks Blockbuster's success means Viacom will show double-digit earnings in the third quarter. He says it will be a big money-maker for eight years at least.

Viacom's cable-TV systems are being sold for \$2.3 billion in a stock-swap deal to Tele-Communications (TCI). The sale cuts \$1.7 billion from Viacom's \$11.4 billion debt and reduces the number of shares," says McAlpine. The sale will let shareholders trade Viacom stock for TCI Pacific Communications, a unit TCI formed for the deal. McAlpine says the sale gets Viacom out of cable-TV systems—"a big user of cash." Viacom spokesman Carl Foltz wouldn't comment on radio-station rumors.

A PILE OF CHIPS ON THIS CASINO

John Boland, who heads investment firm Remnant Partners, scouts for little-known companies that have undergone restructuring, including bankruptcy. One find—Riviera Holdings (RIV)—is fast outgrowing such a categorization. The shares have been on a roll, from 8 in February to nearly 15 on July 23—thanks to big buyers. The company owns the 210-room Riviera Hotel & Casino in Las Vegas.

Boland is delighted but not surprised by the surge in interest in Riviera: "It's a very cheap play—in the fastest-growing U.S. city," he says. Boland thinks the stock is worth \$21 based on estimated 1996 earnings of \$2 a share.

But other pros think it may be worth more—in a takeover. Whispers are that Riviera is being eyeballed by larger Las Vegas operators. On June 14, Bidwell Partners, which has acquired 8.3% of Riviera, said it would seek talks to help management "maximize shareholder value." Chuck DiRocco, editor of the Las Vegas newspaper *Gaming Today*, notes a flurry of insider buying. It looks as if takeover interest is building up, he feels. Riviera CEO Bill Westerman says: "We haven't received an offer that is above the value we think the company is worth."

Westerman, who made the 40-year-old hotel profitable after it emerged from bankruptcy in 1993, says the company is performing strongly this year amid a generally slower Las Vegas market. He notes that Riviera's sec-

ond-quarter earnings leaped 56%, to 42¢ a share, from 27¢ a year ago. And revenues climbed to \$41.6 million, from \$37.1 million in the year-ago quarter.

REACHING INTO THE SILICON ABYSS

To get a fix on the damage to technology issues during the deep slump, look at Applied Materials (AMAT), the world's No. 1 maker of wafer-fabrication gear for the semiconductor industry. In 11 months, it lost 62% of its value—falling from 59¢ on Aug. 16, 1995, to 22¢ on July 23, 1996. Who would look at this loser? Some savvy tech watchers are—and they're happily buying.

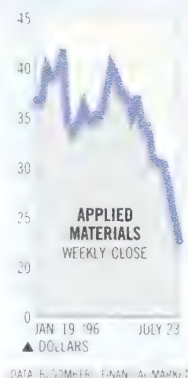
One such pro is Mike Murphy, editor of *California Technology Stock Letter*, who says strong semiconductor demand had kept the price too high. "We've waited a long time to snag this great growth stock," he says. "Now, the Street's obsession with the short term gives us a chance to pick it up cheap."

Applied is cheap by any measure, explains Murphy. It's priced at 1994 levels—although sales and profits have doubled. The only "real risk in buying now is that we may be too early," he says. But the "dynamics are in place for equipment orders to hold up," he adds.

He figures the price will climb to 40 by early next year and to 55 by the end of 1997. It's true, he says, that DRAM producers overdid capacity in 1995, which resulted in a glut of chips and depressed prices: A 4-megabyte chip plunged from \$18 last August to \$3, and a 16-mb went from \$55 in December to below \$10.

But "the risk is in time, not in price," explains Murphy. He thinks demand for semiconductor equipment will pick up sooner than the Street expects. Microprocessor sales, he notes, are driven by personal computers, and PC sales will be driven by cheap DRAM prices, helped by the urge to upgrade PCs to Microsoft's Windows NT. "So to me, Applied should be a core holding in technology," argues Murphy.

A VICTIM OF THE HIGH-TECH SLUMP



TURNAROUND ARTISTS

THIS BOSS IS PREPPED

Kaplan's Grayer recharges the test-preparation company

Jonathan Grayer was already seen as a wunderkind at *Newsweek* when the call came. Within six months of joining the magazine, he had become marketing director—and moved out of the converted supply closet that was his first office. A year later, Alan G. Spoon, president and chief operating officer of *Newsweek's* parent, Washington Post Co., was on the line. "We have a struggling subsidiary called Kaplan, and I would like you to get involved," Spoon said. At 26, Grayer began his second career.

He got involved, all right: Less than three years later, in 1994, he became president and chief executive of Kaplan Educational Centers. Now 31, he's transforming what was a has-been test-preparation company threatened by new competition into a multifaceted education empire (table). "Honestly, I was nervous when we made him president at only 29," says Spoon. "But that feeling lasted for about 16 seconds, because I knew he was exactly the right guy."

"GOING SOMEWHERE." Spoon was first struck by Grayer's energy and brains when he hired the Harvard University business school student as an intern in 1989. Those qualities led Spoon to bring Grayer to *Newsweek* after graduation—and soon persuaded him that Grayer might help fix Kaplan.

Moving there as regional operations director in late 1991, Grayer found a company that, after creating the test-prep business in 1938, had changed little. Since 1981, Kaplan had been challenged by upstart Princeton Review Inc., which was cutting into its market—particularly in SAT preparation—with a hip, irreverent program and ads Grayer claims inflated Princeton students' test-score gains, a charge Princeton denies.

One of Grayer's first moves—a threat to sue over the ads—led to a pact to settle disputes through arbitration. Next, Grayer started hiring, signing up so many Harvard MBAs that the staff roster soon re-



LEVERAGING: Grayer, 31, is turning laggard Kaplan into an education empire

sembled that of an investment bank. "He would get you to say, 'You know something? I'm going to leave a great job and a great situation to take what appears to be a step down,'" says Executive Vice-President Andrew S. Rosen, who moved from *Newsweek* because "I knew this company was going somewhere and that Jonathan was going somewhere, too."

Where Grayer was going was to the top. Promoted to vice-president for marketing, he got Kaplan into publishing books—an area where Princeton was flourishing. After publishing its first books with Bantam Doubleday Dell Publishing Group Inc., Kaplan this year moved to Simon & Schuster Inc., which created a Kaplan Books imprint.

Named president and CEO two years ago, Grayer began updating the core business. He launched Kaplan Interactive to sell software and online services, another area pioneered by Princeton. And he created an ad strategy focusing on nontraditional media such as New York subways.

Now he's leveraging the Kaplan name

in other businesses. Last year, he purchased Crimson & Brown Associates, a minority recruiting company, and launched Kap-Loan, which uses Kaplan's huge database of students to market student loans from UBL Educational Finance Center. Recently, Kaplan purchased the San Francisco-based Score! Learning Center. It was renamed Score@Kaplan and plans to go national with its after-school enrichment courses for kids in grades K-12.

While Post Co. doesn't break down Kaplan's results, Grayer says revenue rose 8% in 1994 and 11% in 1995, to \$10 million; profits are "well into the millions, seven figures." Notes Spoon: "You can't put into trajectories, but you can't always be certain of landings. Jonathan's always been perfect."

Lately, Grayer has been talking up Kaplan's ventures to Smith Barney and Lehman Brothers Inc. He denies a spin-off is in the works. "We wanted to get the message out that we were independent," he says. Still, Michael Moe, growth stocks director at Montgomery Securities, muses: "I would love to see some kind of spin-out or some way to make this entity separate, because it has a very unique growth opportunity."

Grayer says his goal is "to create an educational institution that gives for-profit education an important place in American life." As for the humble room where his career began: "I had them turn it back into a supply closet," he says.

By Andrew Ross Sorkin
in New York

BEYOND THE SATS

Grayer has expanded Kaplan's products and services:

KAPLAN EDUCATIONAL CENTERS Test-preparation courses

KAPLAN INTERACTIVE Software and online division

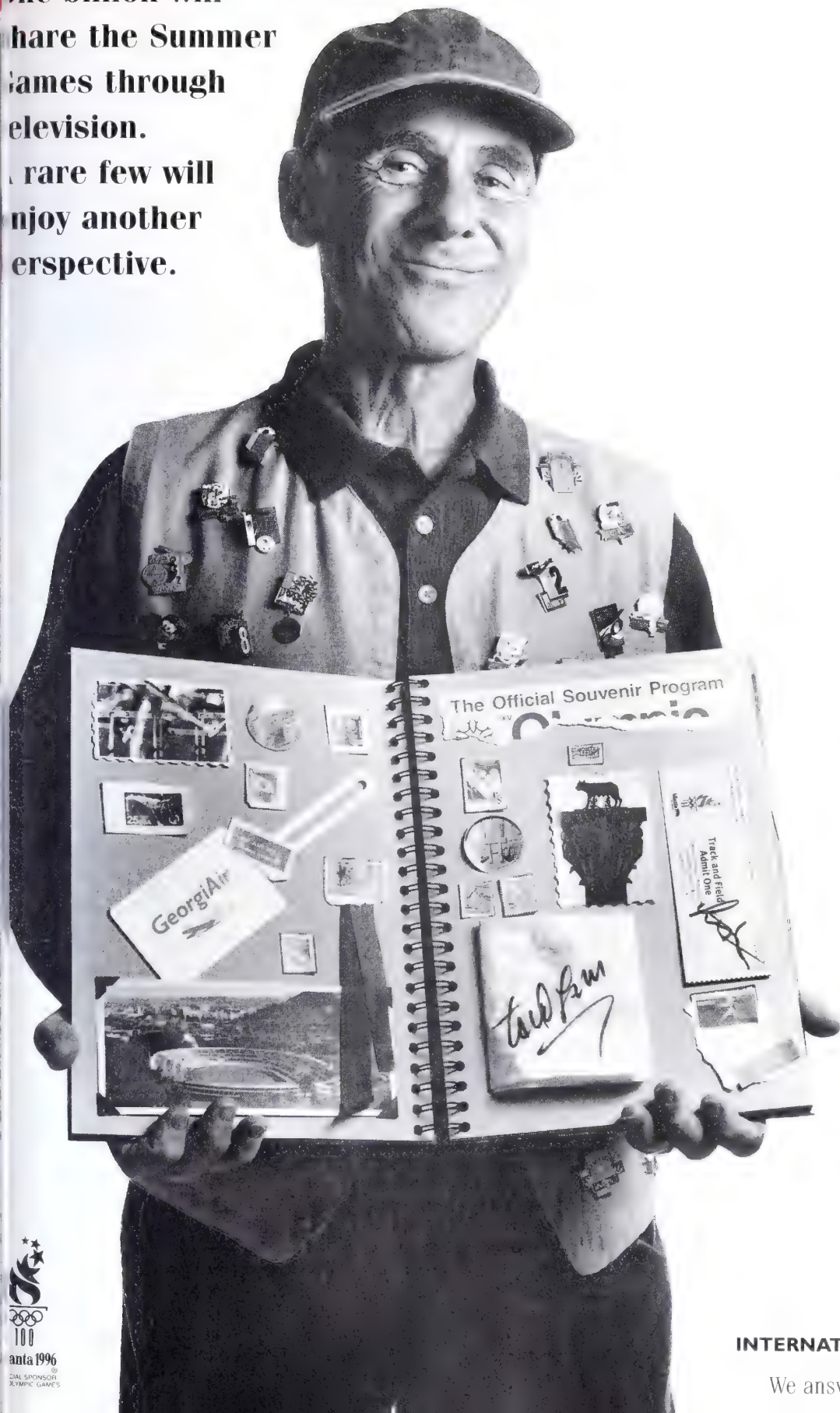
CRIMSON & BROWN Diversity recruiting firm

KAP-LOAN Student loan marketer

SCORE@KAPLAN Enrichment courses for K-12

KAPLAN BOOKS Test-preparation books

One billion will
share the Summer
Games through
television.
A rare few will
enjoy another
perspective.



There will be lots of memorable video moments. Yet, for those able to see the Atlanta Games in person, the most personal mementos will probably be on paper. Those ninth-row tickets to the diving finals. A program guide to the Olympic cultural festival, complete with cappuccino stain. A prized autograph hastily scribbled on a napkin. Perhaps we're biased about the emotional value of paper, given that we produce more kinds than any other company in the world. Then again, we hear scrapbooks are selling briskly.

STARBUCKS DOES NOT LIVE BY COFFEE ALONE

Its name is appearing on everything from ice cream to CDs

One of the first things Scott Bedbury did as Starbucks Corp.'s new vice-president for marketing was learn how to make Frappuccino. The cold blend of ice, milk, and coffee introduced on the West Coast last year boosted local business by 11% in June, July, and August. On a hot day last summer, Bedbury toiled behind a Starbucks counter and found he couldn't make the stuff fast enough for the Frappuccino-frenzied crowd. "I was at that blender all day," recalls Bedbury, who came to the Starbucks marketing job after a seven-year stint as Nike Inc.'s global advertising director. "Now they call me the Seattle frap artist."

Starbucks is hoping for more artistry from the 39-year-old Bedbury. He is pushing Starbucks' name onto grocery shelves through a series of carefully planned joint ventures. The most ambitious: a partnership with PepsiCo Inc. to make a bottled version of Frappuccino that will appear this month in West Coast groceries. "We are reinventing coffee in other categories. My job is to strengthen the brand on all fronts," says Bedbury.

TORRID PACE. Starbucks, which pioneered upscale coffee bars, is still in a fast-growth phase as every crossroads in America gets its obligatory espresso bar. Not all of them belong to Starbucks. But the more people get used to spending \$2 on a cup of coffee, the more Starbucks, the dominant player, benefits. Last fiscal year, which ended in September, sales grew from \$285 million to \$465 million, up 63%. Earnings rose 156%, to \$26 million, 10 times the level in 1991. Still, that torrid pace looks unsustainable. For the first half of fiscal 1996, earnings rose just 4.3%, to \$14.4 million, on a revenue gain of 49%, to \$323 million. "Local competition among coffee stores is tense," says Jean-Michel Valette, an analyst at Hambrecht & Quist. "But Starbucks is the only one out there that has a national level of recognition and awareness."

The company, which expects to grow from 870 stores now to 2,000 by

the end of the decade, has no plans to move away from its core business. But Starbucks is hoping that a strong presence in supermarkets and other outlets will reinforce the brand and drive more traffic into Starbucks stores. In another 50-50 deal, Dreyer's Grand Ice Cream Inc. is distributing five flavors of Starbucks coffee ice cream, such as Espresso Swirl and Javachip, to grocery freezers across the country starting this month. The coffee chain has also col-

STARBUCKS TEAMS UP

PARTNER	VENTURE
PEPSICO	Bottled cold coffee
DREYER'S GRAND ICE CREAM	Coffee ice cream
UNITED AIRLINES	Coffee on board
REDHOOK BREWERY	Coffee-flavored beer
CAPITOL RECORDS	Jazz CDs

DATA COMPANY REPORTS



FRAP ATTACK:
Will the bottled version succeed?

laborated with Capitol Records Inc. on two Starbucks jazz CDs, available at Starbucks stores. And Redhook Brewery, part-owned by Anheuser-Busch Cos., uses Starbucks coffee extract in its Double Black Stout Beer.

Bedbury says the company is interested in other joint ventures with partners that can extend the brand. Although Starbucks is ubiquitous on the West Coast, the company figures only 1% to 2% of the U.S. population has tried the coffee. "Brand extension gives access to new customers and channels of distribution," says Andrew M. Barish, an analyst at Robertson, Stephens & Company in San Francisco.

But the strategy carries risk, too. "There are not a lot of brands that can do both retail and packaged goods," says David Aaker, author of *Building Strong Brands*. "Personality and energy are hard to reinvent in packaged goods at the supermarket." And too many extensions can erode a brand's identity. Bedbury admits that overextending the Starbucks brand is his biggest worry. **TOUGH SELL.** Still, if Starbucks and Pepsi succeed with Frappuccino, the potential rewards are immense. With \$30 billion in annual sales, coffee is the second-largest beverage category, after soda pop. And specialty coffees such as Starbucks are the fastest-growing segment. But while the numbers are irresistible, cold coffee in the U.S. has proved to be an extremely tough sell. Maxwell House's Cappio, pulled from shelves this spring, is just the latest

flop. Mazgran, a carbonated coffee drink that was an earlier product of the Pepsi-Starbucks partnership, failed last year. But Starbucks believes its name is strong enough to power a successful entrant. And it plans to learn from earlier mistakes. Cappio was relegated to the bottom shelf of the coffee aisle, for example. Frappuccino will be sold with other drinks and iced teas, where Pepsi already commands prime shelf space.

Starbucks is not the only one tempted by the prepared-coffee category. This summer, some big names in beverages will give cold coffee a try. Coca-Cola Co. is teaming up to test a coffee drink with Nestlé, its iced-tea partner. Nestlé is also independently test-marketing its six flavors of ready-to-drink coffee only on the West Coast in prime Starbucks territory. With a competitive battle brewing, the Seattle frap artist will have to work hard to keep the Starbucks brand perking.

By Seanna Browder in Seattle

Every day, your lust for cutting edge technology wages war against your unbridled passion to save a buck.



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WHERE ARE THE BOMB SNIFFERS?

The technology exists to make planes safer—but it's costly

If TWA Flight 800 really was blown apart by a terrorist bomb hidden in luggage, then the tragedy is compounded by travesty. Equipment already in the TWA terminal at New York's John F. Kennedy International Airport could have detected such a bomb. Unfortunately, it inspects only incoming luggage, not outgoing. It was installed in April, 1992, by the U.S. Customs Service.

Today, virtually every piece of luggage that enters the U.S. from overseas is screened in the bowels of an international arrivals terminal, but the search is for drugs and drug money, not bombs. "The same equipment could be tweaked and used upstairs to scan outgoing bags for explosives," says Ralph S. Sheridan, president of American Science & Engineering Inc. in Billerica, Mass. AS&E supplies the special X-ray systems to Customs and has already built a modified version for spotting bombs.

At least a half-dozen U.S. companies, plus a few in Europe, now make systems that can detect bombs—including plastic explosives—inside a suitcase or, in some cases, even a cargo container. This equipment is designed to scan luggage that has been checked with the airline, not carry-on bags.

Why aren't some of these new machines being used to inspect checked luggage bound for outgoing flights? In Europe, they are. Some 40 airports have installed U.S.-made equipment, and more have ordered it, because the European Civil Aviation Conference has decreed that all checked baggage must be electronically screened by 2000. Britain hopes to do that by next year.

LONG WAIT. The stuff isn't cheap. Baggage scanners from InVision Technologies Inc. in Foster City, Calif., cost roughly \$1 million apiece. Yet the company has delivered 11 systems in Europe, one in Japan, and three in Israel. In the U.S., its equipment is used by only two airlines—Delta Air Lines Inc. in Atlanta and United Airlines Inc. in San Francisco. Israel's El Al Airlines Ltd. will



THE VISIBLE BRIGAND

An X-ray screener made by AS&E can detect a plastic gun, hacksaw blade, explosives, and knives as well as drugs

put one in its JFK terminal this year.

One reason for the scarcity of this equipment: the Federal Aviation Administration has yet to mandate its use, even though the agency subsidized the development of most systems. The FAA plans to continue field-testing through 2000. So the airlines may not know what will be required until then.

The FAA declined to be interviewed. U.S. airlines almost have to wait for direction from the FAA. In Europe, airport security is the responsibility of a government agency or an independent, for-profit operation such as BAA Plc, which runs seven big British airports. But in the U.S., the airlines themselves handle security. Since security has never been a hot marketing issue, it's doubtful they will spend heavily for systems that may not end up complying with the FAA requirements—especially since the FAA is setting high standards that hike costs.

To minimize the risk of operator error, the FAA has stipulated that the equipment be totally automatic. It has to detect explosives 90% of the time without human help—and produce no more than 10% false alarms. Such idiotproof operation is costly and takes longer to develop. So far, InVision's megabuck system is the only one certified by the FAA. The AS&E X-ray machines used by Customs cost only \$125,000, but they require a skilled operator. An automatic version will run more than \$300,000.

So the FAA is in a bind. As a regulator, it wants every bag loaded onto international flights to be checked for explosives. But the agency figures a bill for that would be \$400 million a year, \$2 billion just for the country's 75 major airports. Wearing its other hat as a promoter of aviation, it seems reluctant



force airlines to lay out such huge sums.

Airline security experts praise the FAA for stimulating the development of airport security technologies. In the aftermath of the 1988 downing of Pan Am Flight 103 over Lockerbie, Scotland, Congress directed the FAA to come up with answers. The agency spent more than \$120 million on 40 programs aimed at upgrading

ity measures that hail from an era of hijackers with metal handguns and vests were the threat. Now, systems that detect a few ounces of plastic explosive rolled out flat to look like a suitcase lining.

Quantum Magnetics Inc. in San Diego used \$600,000 of FAA money to develop a "sniffer" based on magnetic resonance imaging (MRI) medical technology. It emits radio waves that stimulate only the cigar- or disk-shaped nuclei common in molecules of explosives. Quantum Chairman Lowell J. Bennett: "We actually detect the explosive," not substances with a high oxygen content, which might or might not be bombs.

INIC. After Thermedics Inc. in Woburn, Mass., got \$7 million from the FAA and another \$7 million from the State Dept., it came up with a gadget that finds just a few molecules of explosive on a terrorist's shoes or hands. Nine of these \$165,000 devices are in use at airports in 11 foreign countries. The company has been testing them for two years. "It's ironic," says Thermedics President John W. Wood Jr. "If you had to be screened with the latest in explosive-detection technology, you'd fly out of a European airport."ivid Technologies Inc., also in Woburn, has a twin-beam X-ray system that excites molecules to determine their chemical composition of objects in a bag. They are in service at 20 European airports. Pittsburgh's Mine Safety Appliances Co., which makes mine-gas detectors, has a prototype of what it calls the fastest nose in the West—developed jointly with Siberia's Institute of Design Engineering, which pioneered the bomb-detection technology used by the KGB. And AS&E, in addition to its explosive detector, has adapted X-ray technology for body scans. It adds Superman-type vision to spot plastic bombs and plastic weapons concealed under clothing (photo). That adds up to a virtual strip search, but the company is betting that Americans will pay off modestly for safety.

Travelers might also be willing to pay a couple of extra bucks for more security. Several congressmen favor a 1% surcharge on airline tickets to subsidize new baggage-inspection systems, just as a similar flying tax funded modernization at Customs. It could come too soon for David M. Pillor, vice-president of InVision. "We're going to spend \$1 per ticket on customs and immigration, and 50¢ a ticket for agricultural screening to look for ap—but nothing for this?" Makes you wonder about Washington's priorities.

By Otis Port in New York, with bureau reports



SGS CLEAN ROOM:
Sustaining the pace won't be easy

share of the global chip market to jump to 5% by 2000, from 2.2% at the end of last year. That puts SGS-Thomson, with annual sales of \$4 billion, on track to join the ranks of the world's 10 largest semiconductor companies, now occupied by only one other

ELECTRONICS

MAKING HAY IN THE RAIN

As its industry slumps, SGS cashes in on specialized chips

During his 35 years in the semiconductor business, Pasquale Pistorio has seen some punishing market contractions as the industry has gyrated through eight business cycles. But the supply glut of 1996 will always make the CEO of SGS-Thomson Microelectronics smile. While a global excess of memory chips is thrashing industry earnings in mid-July, the French-Italian chipmaker happily reported that second-quarter profits spurted 44% on a 19% increase in sales—driving the share price up 10%.

How did Pistorio pull this off? By carving out a strong foothold in new markets for customized chips—the type that control cellular phones, automobile air bags, ink-jet printers and high-function televisions. These devices are stepping stones to chips that contain entire electronic systems. Unlike Siemens and many Asian competitors, Pistorio steered SGS-Thomson away from standard memory chips, now in severe oversupply. "Their product strategy is clearly working," says Peter Knox, semiconductor analyst with UBS Ltd.

Market researcher Dataquest Inc. concurs. It ranks SGS-Thomson No. 1 worldwide in four chip categories and expects the company's

European chipmaker, Philips Electronics. "SGS-Thomson is outshining a lot of companies," says Dataquest semiconductor analyst Mike Williams. "They have a very balanced portfolio."

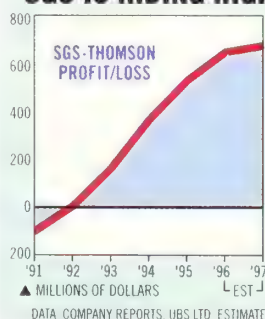
Nobody expected this in 1987, when SGS-Thomson was formed by the merger of two money-losing French and Italian state-owned chipmakers highly dependent on national subsidies for survival. That's when Pistorio, a former Motorola Inc. executive, boldly set his sights on an emerging market for application-specific integrated circuits, or ASICs—the partly customized chips that manage everything from car engines to computer printers.

BIG GAMBLE. Working with customers such as Nokia Group in mobile communications and disk drive giant Seagate Technology Inc., SGS-Thomson pioneered applications that mix different semiconductor technologies on one chip. Teams from SGS-Thomson now collaborate on TV decoder boxes with counterparts at Thomson Consumer Electronics/RCA and on automotive electronics with Robert Bosch. In Japan, Sony Corp. and Toyota Motor Co. are eager clients. And fast-growing Asia now kicks in 29% of sales, up from 18% five years ago. "Putting systems on silicon is the key issue that will confront everyone in the next five years," says Pistorio.

Sustaining this breakneck pace won't be easy. Competitors in the U.S., Japan, and Asia are all targeting the same types of systems-on-chips. And there is no guarantee that the products Pistorio is betting on, such as digital televisions, will take off as quickly as he envisioned. But SGS has shown that it can march up the ranks of chip powerhouses in good times and in bad.

By Gail Edmondson in Paris

SGS IS RIDING HIGH



INTERNET

ADDRESS DIRECTORY

Adobe Systems Inc.
http://www.adobe.com/?BW

Advanced Micro Devices
http://www.amd.com

Aetna
http://www.aetna.com

America West Airlines
http://www.america-west.com

The American Institute of Architects
http://www.aia.org

American Power Conversion
http://www.apcc.com

The American Stock Exchange
http://www.amex.com

Ameritech
http://www.ameritech.com

AMP
http://www.amp.com

Andersen Consulting
http://www.ac.com

Apple Computer
http://www.apple.com

Arthur Andersen
http://www.ArthurAndersen.com

AST Computer
http://www.ast.com

AT&T
http://www.att.com

Bavarian Ministry for Economic Affairs
http://www.bayern.de

Bell Atlantic
http://www.bell-atl.com

Cadillac
http://www.cadillac.com

Canon
http://www.canon.com

Chase
http://www.chase.com

Chevrolet Motor Division
http://www.chevrolet.com/car

Chrysler
http://www.chryslercorp.com/

Cisco Systems
http://www.cisco.com

Cobra Golf
http://www.CobraGolf.com

Compaq
http://www.compaq.com

Computer Associates
http://www.cai.com

Con-Way Transp. Services
http://www.con-way.com

Consolidated Freightways, Inc.
http://www.cnf.com

Delta Air Lines
http://www.delta-air.com

Deutsche Telekom
http://www.dtag.de

Digital PC
http://www.pc.digital.com

Diners Club International
http://www.dinersclub.com

Exide Electronics
http://www.exide.com

Emery Worldwide
http://www.emeryworld.com

EIS International
http://www.surefind.com

Federal Emergency Management Agency
http://www.fema.gov

FedEx
http://www.fedex.com

Florida Power & Light
http://www.fpl.com

Ford
http://www.ford.com/

Fujitsu
http://www.fujitsu.com

Fujitsu PC Corporation
http://www.fujitsu-pc.com

Gateway 2000
http://www.gw2k.com

GE Information Services
http://www.geis.com

General Motors
http://www.gm.com

Hewlett-Packard
http://www.hp.com

Hilton Hotels
http://www.hilton.com

Honda
http://www.honda.com

IBM
http://www.ibm.com

Informix
http://www.informix.com

Intel
http://www.intel.com/

Intersolv
http://www.intersolv.com

International Institute for Management Development
http://www.imd.ch/

ITT Hartford
http://www.itthartford.com

Janus Funds
http://network.galt.com/janus

Kingston Technology
http://www.kingston.com/bw.htm

Kinko's Corporate
http://www.kinkos.com

Kodak
http://www.kodak.com/

Lawson Software
http://www.Lawson.com

Lexus
http://www.lexususa.com

Lincoln-Mercury
http://www.lincolnmcury.com

Lotus
http://www.lotus.com

MAG Innovision
http://www.maginnovision.com

MCI
http://www.mci.com

Mercedes-Benz
http://www.usa.mercedes-benz.com

Merrill Lynch
http://www.ml.com/

Microsoft
http://www.microsoft.com/

Motorola, Wireless Data Group
http://www.mot.com/wdg/

Netcom On-Line Communication Services
http://www.netcom.com

Novell
http://www.novell.com

Ohio Department of Development
http://www.ohio.biz.com

Okidata
http://www.okidata.com

Omron Corp./North America
http://www.omron.co.jp

Oracle Corporation
http://www.oracle.com

Origin
http://www.origin.nl/

PageNet
http://www.pagenet.com

PeopleSoft
http://www.peoplesoft.com

The Principal Financial Group
http://www.principal.com

PSINet
http://www.psi.net/

Raytheon
http://www.raytheon.com

Roberts Express, Inc.
http://www.roberts.com

Charles Schwab
http://www.schwab.com

Saab
http://www.saabusa.com

SAP
http://www.sap.com

SAS Institute
http://www.sas.com/

Sequent Computer Systems, Inc.
http://www.sequent.com

Siemens
http://www.siemens.com

SkyTel
http://www.skytel.com

Sprint
http://www.sprint.com

Sun Microsystems
http://www.sun.com

Swissair
http://www.swissair.com

Symantec
http://www.symantec.com

T. Rowe Price
http://www.troweprice.com

Texas Instruments
http://www.ti.com

Toshiba America Information Systems
http://www.toshiba.com

Toyota Motors
http://www.toyota.com

Unisys
http://www.unisys.com

United Airlines
http://www.ual.com

U.S. Robotics
http://www.usr.com

UPS
http://www.ups.com

The Vanguard Group
http://www.vanguard.com

Wonderware Corporation
http://www.wonderware.com



Sun designed the first intranet back when people thought intranet was a typo.



http://www.sun.com

Developments to Watch

EDITED BY NEIL GROSS

CLOTH THAT GLOBBERS GERMS

SOMETIMES THE KITCHEN SEEMS LIKE A war zone. Raw chicken could leave salmonella smears on the cutting board, and that germs might be dripping from the raspberries. No wonder business is booming: Microban Products Co. in Huntersville, N.C. Since 1990, it has been supplying manufacturers of hospital gear with antimicrobial chemical additives. Mixed into synthetic fibers in protective clothing or bedcovers, these pellet-encased additives kill bacteria and fungi on contact. The pellets stay embedded in finished materials, impervious to repeated washing, according to product testers at North American Science Associates Inc., Kennesaw, Ga.

Now Microban is expanding into the home, supplying the pellets to manufacturers of kitchen cutting boards, pillows, sheets, bathroom towels, and mops. Toy-maker Hasbro Inc. is test-marketing children's high chairs with Microban additives molded into the food tray. The treatment adds about \$10 to the price of a \$70 high chair, according to Hasbro. Toys may be next, says the company. One nice feature: Bugs don't seem to build up resistance to these chemicals, which are also widely used in antibacterial soaps and deodorants. And testers at Gibraltar Labs Inc. in Fairfield, N.J., say a battery of tests uncovered no indication of toxicity for humans. □

MEMBRANCE THINGS PAST IN A CHIP

THE FILM *TOTAL RECALL*, with Arnold Schwarzenegger's memory implants seemed pretty far-fetched. But were they? After analyzing the latest trends in neurological and semiconductor research, scientists at British Telecommunications PLC have concluded that in about 30 years, it will be possible to capture data representing all of a human's sensory experiences on a single tiny chip implanted in the brain.

His feat will be possible thanks to advanced circuit-making techniques such as nanolithography, which will drastically shrink circuits on memory chips. By 2025, predicts Christopher S. Winter, research group leader at BT Laboratories, one chip will store some 10 terabytes of information, roughly 1 million times as many bits as today's state-of-the-art chips. Sensory data would be captured via a series of biological probes tapping electrical impulses from up to 1 million of the brain's visual, auditory, olfactory, and taste nerves. Collecting thoughts or emo-



tions may prove to be impossible. But storing pure sensory data is feasible, Winter says, because the fir-

ing of neurons is already a binary, "on/off" phenomenon akin to digital electronics. If such chips were ever developed, applications would literally boggle the mind. People could access an implanted chip to relive experiences, or they might extract and wire it to a computer so that memories could be displayed on a screen. In theory, chips could even be transplanted from one person's brain to another's.

Heidi Dawley

GULPING DOWN A BLOOD-BOOSTER?

THE U.S. BIOTECH INDUSTRY HAS PRODUCED FEW BLOCK-busters like Amgen Inc.'s erythropoietin (EPO), a multibillion-dollar anemia drug. But EPO suffers from a common problem: It's a large molecule that is destroyed by digestion and must be injected rather than swallowed as a pill.

In the July 26 issue of *Science*, researchers at R. W. Johnson Pharmaceutical Research Institute, Affymax, and Scripps describe a possible solution. Using combinatorial chemistry—a technique for shuffling molecular building blocks to create thousands of drug candidates—they produced a protein fragment, or peptide, that mimics the larger EPO molecule but is just one-fifteenth its size. The scientists used the new compound to understand exactly how the chemical binds to—and turns on—the body's EPO receptor. This peptide won't replace EPO, the authors caution. In its current form, it would neither bind strongly to the receptor nor survive digestion. But sturdier varieties could come soon. *John Carey*

INNOVATIONS



■ Scientists at Utah State University have discovered a genetic marker for an inherited trait that bestows meatier hindquarters on sheep and other livestock. Since it was identified 13 years ago, the trait—called callipyge (Greek for "beautiful buttocks")—has baffled scientists: It vanishes and reappears in successive generations of sheep at odd intervals. With the marker, consisting of easily recognized bits of DNA, scientists can create a genetic profile for rams and ewes whose offspring are likely to possess this trait.

■ Cable modems will allow high-speed Internet browsing over coaxial cable. But the service will be available only in neighborhoods with up-to-date cable-TV networks and will add about \$30 per month to cable bills. WorldGate Communications in Trevose, Pa., says it can provide similar functions over cable for just \$4.95 a month. Rather than hijack a whole cable channel for Internet browsing, WorldGate says its two-way TV On-Line service will run over empty spaces in occupied channels, namely the "vertical blanking interval" between picture frames. The download speed: 100 kilobits per second. That's slower than a cable modem but three times faster than modems on phone lines, the type of service that rival WebTV Networks Inc. plans to use.

JACK WELCH'S CYBER-CZAR

Can Gary Reiner make GE's info-technology bet pay off?

In his five years as a trusted lieutenant to General Electric CEO John F. Welch, Gary M. Reiner has handled many critical assignments. He has overseen efforts to accelerate product development, speed up manufacturing, and shorten supply lines. And he has headed one of the corporate strategy groups that Welch uses to make sure his management ideas translate well to the shop floor and office cubicle.

But the task that Welch handed the intense but personable Reiner in April may be the biggest challenge yet for the former Boston Consulting Group partner. Reiner, 42, has been named chief information officer, General Electric Co.'s first corporate computer czar in many years. He will be Welch's point man for integrating GE's many far-flung investments in information technology. GE won't say, but *Information Week* estimates that the company spent some \$758 million on computers and communications in 1995. GE also is a traveler on the Information Superhighway. The company has been selling electronic communications through its GE Information Services (GEIS) unit for years and, with MSNBC, the new cable-TV network and Web site its NBC unit just launched with Microsoft Corp., it's now in new media.

BRAINSTORMS. But like other enterprises, GE hasn't gotten the payoff it expected from its technology investments. One reason: While its dozen businesses all have technology officers, the corporation hasn't focused on using computing strategically—at least not with the same zeal with which Welch has pushed to pare the roster of suppliers or generate free cash flow, for instance.

Until now, Reiner's job is to get GE on the cutting edge—from equipping its sales personnel with the latest technology to building self-diagnosis into industrial machines to using the Internet to buy and sell spare parts and plastics, for instance. "I've got to make [information technology] a competitive advantage for GE," says Reiner.

More important, by appointing Reiner, whose specialty at Boston Consulting was automation, Welch has made it clear that computing is no longer just a support function, but a key means for hitting corporate goals. "I need somebody who isn't a techie," says Welch. "I need somebody who can make it flow." Says Forrester Research Inc. senior analyst Blaine Irwin: "Welch is very fired up about it. He understands how technology can be leveraged."

Using technology to share ideas across GE is key to Reiner's mission. He has visited every major business unit since his April appointment to see firsthand how each uses computers. In addition, he is holding quarterly brainstorming sessions for all the unit technology officers.

GE also is making extensive use of a new corporate intranet, an internal Internet setup that connects the networks



POINT MAN: Reiner's mission is to harness the power of the Internet

within each division. A GE employee at the motors business in Fort Wayne, Ind., for example, can use the intranet to find out how buyers in other divisions rate a potential supplier. To help draw employees into using the system,

E-SOURCING: 'A CHEAPER WAY OF DOING BUSINESS'

At Anson Machine & Manufacturing in Louisville, computer-aided-manufacturing supervisor Dean Deakins believes in technology's power to change the nature of business. Each year, his metal-fabrication shop sells "tens of millions" worth of parts to General Electric Co.'s aircraft-engine unit. In early 1995, when GE's purchasing people invited him to use a new bulletin board system to bid for that business, Deakins signed on—and soon found other potential customers within GE. "Before, I didn't know GE built locomotives," he says. Today, Deakins is doing between \$1 million and \$2 million a year with the locomotive group.

Now, he is signing up as one of the first to use a World Wide Web-based version of that service. It's the Trading

Process Network, and it's the first series of Internet-based services for electronic commerce that GE's Information Services Div. has in the works (table). In the past, GEIS has delivered services over its own private net-

WAKING UP TO THE WEB

How GE Information Services is using the Internet for electronic commerce:



GE COMPUTES THE FUTURE

Led by Gary Reiner, its new chief information officer, GE is:

- Encouraging suppliers and customers to do business with it over the Internet
- Developing systems to remotely diagnose problems in everything from jet engines to household appliances
- Creating commercial information services based on systems that have been used internally
- Reengineering its purchasing systems to gain companywide buying power
- Cleaning up key databases to reduce inaccuracies and redundancies

her resignation in late June. With its private computer network, GEIS has deep experience in setting up paperless links between suppliers and their customers worldwide—a technology called electronic data interchange (EDI). The challenge now is to harness the bustling, low-cost, and very public Internet as an electronic-commerce medium, both to help GE and as the basis for new services that GEIS can sell to others.

BARGAIN HUNTING. After a year and a half of testing, GE has started to move its purchasing activities to the Internet. In June, it went live with a setup called the Trading Process Network, which helps match buyers throughout the company with suppliers of everything from refrigerator handles to printer paper (box). GE expects to purchase at least \$1 billion worth of its goods this way in 1996 and 50% of the total by 2000. The payoff, according to Orville A. Bailey, manager of purchasing and supplier productivity solutions, is that GE can select from a broader base

of suppliers as well as cut its purchasing costs. Plus, the setup will help GE, already famous for getting price concessions from suppliers, to drive an even harder bargain by pooling orders from across its units and winning higher volume discounts.

Reiner has many other plans afoot. Service technicians at the aircraft-en-

gine unit, for example, now scan parts data and diagrams on laptop computers, instead of lugging around printed manuals. "But that's not ubiquitous within GE," Reiner says. So through the quarterly technology councils and spin-off subgroups, Reiner will prod other businesses to follow suit. "If we encounter a best practice in one of our businesses, a person from that business would get up with charts and show the others how," says Reiner. GE Medical Systems, for example, has a program that dials into magnetic resonance imaging (MRI) machines and remotely diagnoses faults, in some cases before they cause trouble. Now, that same setup is being adapted to other products, starting with turbines for generating electricity and extending to jet engines and motors.

Another key task Reiner must tackle is to bring some order to GE's internal databases and software. By setting standards for how each business unit should organize its customer databases, for instance, the units' data may be more easily combined to yield new marketing intelligence. A customer buying GE's plastics, for instance, might also be found buying its light bulbs. Plus, Reiner is leaning toward purchasing more packaged software vs. developing systems in-house. "Why reinvent the wheel?" he says.

Why, indeed, when you've got a more pressing assignment from Jack Welch: reinventing the way this \$70 billion company uses information technology.

By Tim Smart in Fairfield, Conn.

ome page displays a particularly ar piece of data: GE's current stock

haps Reiner's most important s will be in electronic commerce. now reports directly to Reiner. a former aide of his, Harvey F. ers, has replaced GE veteran Hel-S. Runtagh as its head, following

ding Process Network lets electronically download GE's or proposals, view diagrams efications, and communicate anagers, who together plan to stem rolling by purchasing worth of items this way in tually, "it will be our main munciations with suppliers," rt Livingston, who as head of sourcing for the GE Lighting ees annual purchases of

\$2 billion worth of supplies. Enthuses Deakins: "There'll be a whole lot less flying people places and less talking back and forth. It's going to be a cheaper way of doing business."

GLOBAL MARKETPLACE. Cheaper, certainly, for GE, which buys \$50 billion a year worth of components, materials, and services. Since experts reckon that it typically costs \$50 to process a paper purchase order but only \$5 in electronic form, GE stands to save millions. Plus,

electronic purchasing fits with the edict by Chief Executive John F. Welch to improve the efficiency and accuracy of all internal processes, a quality-management effort dubbed Six Sigma. Going on the Web, says Livingston, will "take our processing time down by one third."

GEIS is taking the Trading Process Network global, signing up companies everywhere that might want to trade with one another. Eventually, GEIS officials say, the setup could evolve into a full-blown, global electronic market—perhaps with GE collecting a fee from every transaction. For now, it's just helping GE and other companies locate and solicit bids from a broader range of suppliers—some 10,000 by yearend, according to company executives.

Eventually, companies all over the world may discover what Deakins has learned: There are untold sales opportunities at the \$70 billion giant—once you get an electronic foot in the door.

By Tim Smart in Fairfield, Conn.

BUSINESSPRO

For small businesses, it bundles E-mail, videoconferencing, and other electronic services with discounts on express mail and car rentals

CORPORATE PURCHASING

Joint ventures with Netscape Communications and Thomas Publishing will create intranet-based catalogs and ordering systems

SECURE WEB TRANSACTIONS

New software provides secure access from the World Wide Web to GEIS's private electronic data interchange network

DATA. BUSINESS WEEK

for companies qualify suppliers



SOFTWARE

CRAZY LIKE A FOX—OR JUST CRAZY?

Armed with WordPerfect, Corel's Cowpland takes on Microsoft

Michael C.J. Cowpland is easily Canada's most flamboyant entrepreneur. Last year, the chief executive of Canada's No. 1 software company, Corel Corp., riled the sedate Rockcliffe section of Ottawa by building a 20,000-square-foot glass-walled mansion for his second wife, Marilyn. Its 10-car garage houses a Lamborghini and a pair of his-and-her Porsches. Last December, Marilyn caused a stir by posing for the cover of *Ottawa Magazine* in a skintight spandex Santa suit.

Cowpland's audacious style is matched by his outsize ambition for Corel: to transform it from a niche player to a software powerhouse with \$1 billion in sales within three years. To do it, Cowpland is betting he can revive WordPerfect, the once-leading supplier of word-processing programs that Corel bought from Novell Inc. in March.

MASTER PLAN. That, however, puts Corel on a collision course with Microsoft Corp., the \$8 billion giant that has 90% of the market for software "suites"—the bundles of office applications that businesses use. "I don't think he picked the right competitor to go up against," says David

W. Wright, director of research at Toronto's Marleau, Lemire Securities. Corel stock, meanwhile, is trading at less than half its 52-week high of \$19.

Cowpland argues that he saw "a one-shot opportunity" to snag 20 million WordPerfect customers and the price was right. Corel paid \$158 million—just \$11 million in cash—for businesses Novell had acquired for more than \$1 billion in 1994. Of course, there was a reason for the fire-sale price. WordPerfect's annual sales had slid to \$407 million, from \$629 million in 1993. Its share in suites stood at a paltry 3.6%.

Cowpland figures he can reverse that. "People are ready for an alternative to Microsoft," he declares. In May, he introduced a new suite pairing WordPerfect and Corel programs for Windows 95. Now he's pushing to leapfrog Microsoft with software for the Internet. For example, an office suite due this fall will be written in

FLASH: Cowpland, chief of Canada's Corel, and wife, Marilyn, in their Lamborghini on their wedding day in 1992

Sun Microsystems Inc.'s Java language so it can run on as well as on the scaled-down "work computers" ing developed companies such Oracle Corp.

This isn't the time Cowpland, has bet his career

long odds. In 1973, the young semiconductor engineer co-founded Mite maker of phone equipment, figuring could outmaneuver AT&T and Northern Telecom. Sales soared to over \$250 million before losses forced the partner to sell out to British Telecommunications PLC.

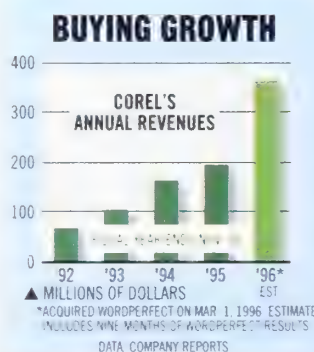
Using \$10 million of his own money, Cowpland quickly launched Corel. Draw, a graphics illustration program, came out in 1989, and Cowpland away the competition with a strategy frequent upgrades, lowball pricing, extravagant promotion. CorelDraw success helped propel Corel revenue to \$196 million last year.

Now, Corel's graphics business stalled. Because customers have been slow to upgrade to a Windows 95 version of Draw, sales are expected to drop to \$90 million this year from around \$150 million in 1995. Cowpland says Draw should rebound in 1997 but concedes that his core market is maturing.

SUITE SUCCESS. So Cowpland is betting on new products including desktop video conferencing. But most of his chips are on WordPerfect. The ever-competitive executive, who played in the Wimbledon finals of Britain's 1995 National Singles tennis tournament, vows he'll grab a share of the suite market. He has cut the price of upgrading to the Corel suite to undercutting Microsoft Office by as much as 50%. Now he's pumping a profit-busting \$100 million into marketing.

The strategy is already showing results. In June, retail sales of the suite jumped 400%, to 800,000 units, matching Office sales, according to Data. But Corel trails Microsoft in key corporate markets. Meanwhile, Cowpland is focusing on the "It's much easier [emerge] as a leader in a brand new field," says. A little chutzpah doesn't hurt, either.

By William Symon
in Ottawa



These Classics Won't Last Forever.



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Site of the Canon Greater Hartford Open, Cromwell, CT



TPC AT SOUTHWIND - September 16
Site of the FedEx St. Jude Classic, Memphis, TN

Unfortunately, not all classics last forever...especially these One-Day PGA TOUR Partners Classics! Normally these Classics are reserved for PGA TOUR Partners, but now we're inviting readers of *Business Week* to join the excitement — and discover what being a Partner is all about. Each Classic is only \$295 and includes: 18 holes of flighted, individual stroke play; pro-scoring; greens fees; a continental breakfast; on-course beverages; an awards luncheon; golf contests; a PGA TOUR money clip and more. You can sign up for one or both of these Classics and you can make your own foursome — even if your partners are not all PGA TOUR Partners. *But you'd better hurry because space is limited!* Call 1-800-742-8687 to experience PGA TOUR Partners tournament play in the 1996 One-Day Partners Classics.

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EDITED BY AMY DUNKIN

KID-FRIENDLY WEB SITES EVEN PARENTS CAN LOVE

When she grows up, 11-year-old Blossom hopes to become a writer, a scientist, or a beauty-salon worker. Cleo, who is 9, wants to be a "veterinarian." And 14-year-old Cassie seeks a job where she "can hang out and surf the Internet all day."

These and lots of other kids are already claiming the World Wide Web as their own. The youngsters jotted down their career aspirations in response to a question posted in the KnowZone section of Jam!z (<http://www.jamz.com>), an online clubhouse aimed at ages 8 to 14. Among the other recent topics in KnowZone was a discussion of staying healthy. "Eat your vegetables, dude and dudettes!" advised a 9-year-old girl. But a 14-year-old boy took a different tack: "I hate eating food that's good for me! Spinach sucks."

HODGEPODGE. For all the talk of the Internet as a deleterious destination for children, the Web is emerging as a vast and—with reasonable parental precautions taken—amusing and educational playground. "The Internet has great resources for kids, as well as resources developed by kids," says Jean Armour Polly, a onetime librarian and author of *The Internet Kids Yellow Pages* (\$19.95, Osborne/McGraw-Hill.)

Indeed, the Web contains a hodgepodge of materials that may appeal to children of all ages. They can visit a

volcano or NASA, check out an array of museum exhibits, fill in a coloring book, solve puzzles, and get an inside peek at some terrifying roller coasters. Socks, the First Cat, leads a virtual tour of the White House. At the Yuckiest Site on the Internet (<http://www.nj.com/yucky>), kids can read *A Day in the Life of Rodney Roach*, a tale that puts a positive spin on those yucky bugs. PBS Online (<http://www.pbs.org>) includes separate home pages for *Mister Rogers' Neighborhood* and *The Magic Schoolbus*, as well as material for older family members.

Many Web sites feature a not-so-subtle commercial message, though they're not all objectionable. Walt Disney's page is a giant billboard for the company, but kids still might like to download video clips from *101 Dalmatians*, *Mary Poppins*, and other classic movies. Crayola's site (<http://www.crayola.com>) includes a demonstration of how crayons are made. There's a basic animation lesson at the Warner Bros. Online site (<http://www.warnerbros.com>), and Web pages for Tweety Bird and other cartoon characters. Kids can also download "connect the dots" and jigsaw puzzles, though they'll need Macromedia's Shockwave plug-in software to take advantage of these multimedia games.

Schools have a growing presence on the Web. Many elementary and secondary institutions maintain pages that allow students and teachers to speak out about topics that concern them. Some sites also offer assistance for projects and term papers. The MAD Science Network (<http://med.wustl.edu/~ysp/MSN/>) is for children, or anyone else, that matter, submit questions to graduate and medical students at Washington University in St. Louis on subjects such as astronomy, botany, and genetics. ("How old is the oldest tree, and what kind is it, and where is it growing?" asked one visitor.) In many sites, kids can change ideas and opinions with pen pals around the planet.

FILTERS. Of course, "talk to strangers" takes on a whole new meaning in cyberspace. Because of the nature of the Web, unsupervised kids may end up clicking on links that transport them to inappropriate territory. So as in a playground, parents should not let the little ones wander off too far online themselves. Whenever possible,



parents should check Web pages before the kids do. They should sit with small children at the computer. And they may even want to restrict their old kids' access to the Net using a filtering program, such as SurfWatch software from Spyglass (800-458-6600) or Cyber Patrol (800-828-2608) from Microsystems Software (BW—Feb. 12). America Online, CompuServe, and other commercial online services let parents block certain areas to kids.

Be especially careful in chat rooms and chat areas, says Julie McKee, author of *Safe Surfing: A Family Guide to the Net* (\$24.95, AP Professional). That's where pornographic or violent material is likely to be found, and unsavory characters most often congregate. McKee urges parents to monitor their kids never reveal their E-mail or home address, phone number, last name, or other personal data.

Some of the frustrations grownups have in using the Web may be due to intolerance for kids' short attention spans. Regardless of Internet speed, many Web sites can be painfully slow. And when graphics take a lot of time to load, young children can't sit through them, says McKeehan. "They don't know what's coming, they don't know what's coming, what's coming..." That said, snazzy graphics may appeal to some kids, so discovering the proper balance may require some trial and error.

W AND TELL. Indeed, finding kid-friendly Web sites isn't much easier than finding grownup sites, which is the reason some parents prefer to stick to the kids' fare offered on AOL, CompuServe's family wow! service,

Where Small Fry Can Surf the Net

WEB SITE/ADDRESS (HTTP://)	COMMENTS
STEVE AND RUTH BENNETT'S FAMILY SURFBOARD www.familysurf.com	Includes treasure hunts, puzzles, and games, an electronic kids' soapbox, and parent resource center.
DISNEY www.disney.com	Fine commercial site lets kids download sounds, pictures, and video clips of favorite Disney films.
INTERNET PUBLIC LIBRARY www.ipl.org	Math and science projects, writing contests, plus picture storybooks such as <i>The Tortoise and the Hare</i> .
KIDSCOM www.kidscom.com	Kids can seek pals with similar interests, post pictures and stories about pets, and write on online graffiti wall.
MAYAQUEST INTERACTIVE EXPEDITION www.mecc.com/mayaquest.html	Software publisher MECC guides kids through an interactive expedition to ancient Mayan civilization.
SPORTS ILLUSTRATED FOR KIDS ONLINE pathfinder.com/@dgHGhQYAuPYJOxec/SIFK/	Magazine articles, trivia, comics, and online interviews with sports heroes.
UNCLE BOB'S KIDS' PAGE gagme.wwwa.com/~boba/kidsi.html	Contains seven sections of annotated links to other sites for kids of all ages and their parents and teachers.
VIRTUAL SCHOOLHOUSE www.sunsite.unc.edu/cisco/schoolhouse.html	Educational links by subject, teaching resources, schools and universities, museums, and libraries.
WEB66: web66.coled.umn.edu/	Project to introduce technology into schools. Contains links to home pages of K-12 schools and items of interest for educators and students.
WHITE HOUSE FOR KIDS www.whitehouse.gov/WH/kids/html/home.html	Socks, the Clinton family cat, guides youngsters through the history of 1600 Pennsylvania Avenue. Includes a look back at First Family kids and pets.

DATA BUSINESS WEEK

Parents who go the Internet route (which they can also do via the commercial online services) can call upon the usual Internet search engines in finding children's sites. Yahoo! has a special version for sites designed for 8- to 14-year-olds called Yahoo!igans! Kids can search by topic (school bell, sports and recreation, science and oddities). Berit's Best Sites for Children (<http://www.cochran.com/theosite/ksites.html>) contains links to other Web pages that are rated on a five-point

scale. Jean Armour Polly's Fifty Extraordinary Experiences for Internet Kids (<http://www.well.com/user/polly/ikyp.exp.html>), from the *Yellow Pages* author, and Uncle Bob's Kids' Page are also decent places to begin your query.

Landing on suitable Web sites should be only the first step. Steve Bennett, who runs the Family Surfboard site, believes "the real learning starts when you turn the computer off." Bennett says that after youngsters visit

KidNews (<http://www.vsa.cape.com/~powens/Kidnews3.html>), a free news service for students and teachers, they might clip articles from newspapers and magazines, tape them to the refrigerator, and hold weekly "editorial sessions" with family members. Or, kids who check out the Global Show-n-Tell page (<http://www.telenaut.com/gst>) where a California condor and red-spectacled parrot are currently on display, should be encouraged to follow up with a family show-and-tell evening.

MAKING PAGES. The ultimate show-and-tell vehicle for the children may be Web pages that they create and post themselves. Microsoft's \$35 Creative Writer 2 for Windows 95, scheduled to debut in September and aimed at 8-year-olds and up, includes features that will let kids easily publish their own Web pages. Similarly, Vividus' \$30 Web Workshop for Apple Macintosh and Windows comes with easy-to-use paint tools, background images, and clip art. Kids can also record their own voices and automatically add links to Yahoo!igans! and Kids Clubs displayed on Vividus' Web site (<http://www.vividus.com>). By pushing a button, children can publish the pages on their Internet

service provider. They can also download free software for creating rudimentary pages on services such as America Online.

The World Wide Web can already help children stimulate their minds and connect with new friends. But just like adult-oriented material, kiddie content on the Internet is still in its infancy. As the offerings become faster and more compelling, you may find that one computer for the family is no longer sufficient. *Edward Baig*

GO EAST, INTREPID INVESTOR

The bull market in U.S. equities is showing signs of severe fatigue, but that doesn't mean you have to forfeit those double-digit gains you've grown accustomed to. However, you may have to start looking in a different direction: east. No, not to the much-acclaimed markets of Southeast Asia but to the booming bourses in Eastern Europe.

Over the next five years, emerging markets in general are expected to be the best-performing asset class, according to a KPMG Peat Marwick survey. Poland, Hungary, the Czech Republic, and yes, even Russia, should lead the pack, offering phenomenal growth at low multiples. Many of the public companies currently have a price-to-earnings ratio of around 7.5 and an earnings-per-share growth rate of 35% to 40% annually. "This is a historic window of opportunity for investors. Returns are excessively high, and valuation levels are extremely low," says Arpad Pongracz, manager of Vontobel Eastern European Equity Fund, the only open-end mutual fund to focus solely on the region. Since the fund's inception in February, Vontobel is up almost 37%.

NO LOCKSTEP. The recent instability of the U.S. market has reinforced the importance of diversification, especially overseas. "Eastern Europe, notably Poland, is a compelling way for investors to hedge the U.S. stock market or redeploy profits," says Suzanne Patrick, a senior analyst for Central European research at Arnhold & S. Bleichroeder in New York. Although these markets were

down slightly the week of July 15 in reaction to the volatility in U.S. stocks, Merrill Lynch research shows that long-term correlation between Eastern Europe and the U.S. appears low.

Investing in Eastern Europe is also a way to play the dollar's strength. With growth in gross domestic product



COMFY: THE CZECH SITE

Foreign Finance Web Sites

CZECH REPUBLIC

<http://www.czech.cz>

HUNGARY

<http://www.fornax.hu/fmon/stock/betaddata.html>

POLAND

<http://info.fuw.edu.pl/pl/poland-text.html>

RUSSIA

<http://www.fe.msk.ru>
<http://world.std.com/~rusport/>

DATA BUSINESSWEEK

ranging from 4% to 6%—almost double that of the U.S.—Poland, Hungary, and the Czech Republic are increasing exports to dollar-based world economies at a

rate faster than industrialized Europe, says Douglas Johnson, senior strategist at Merrill Lynch in New York. For example, Poland's exports to the U.S. over the past two years have been growing at an annual rate of 27%, compared with the 11% average for the major European economies.

Granted, developing Europe and Russia are not for the skittish. "Anyone who invests in these markets really has to be a long-term player," says Richard Saler, manager of Lexington Worldwide Emerging Markets Fund, which presently has a 15% stake in Eastern Europe and year-to-date returns of 9.07%. "The fundamentals can be good, and the market can still go down 10% to 20% on any given day," Patrick Smith, manager of the Pioneer Europe Fund and one of the first money managers to take a big position in the former Eastern bloc, made 100% in 18 months. Content with those results, he has already cashed out.

FEW PURE PLAYS. But others are just jumping in now. Hoping to capitalize on the growth of Russia's burgeoning free-market economy, Lexington Management and Troika Dialog Asset Management in Moscow launched the first open-end Russia fund—the Lexington Troika Dialog Russia Fund—immediately after President Boris Yeltsin's reelection in July. The most volatile emerging market, Russia is up 85.53% in dollar terms so far this year, according to the ASP General Price index.

For now, pure plays are few. American Depository Receipts (ADRs) that allow direct investment are hard to come by. GUM, a Russian retailer, is

one trading currently. Arnhold & S. Bleichroeder, which this fall is placing its first Polish ADR, Mostostalport, a construction holding company—anticipates more will follow in the year. While there are a handful of single-country clo-

The East Booms

INDEX	TOTAL DOLLAR-BASED RETURNS YEAR TO DATE*	TWO-YEAR RETURNS
CZECH REPUBLIC	28.87%	-15.8%
HUNGARY	84.87	38.2%
POLAND	52.18	-10.5%
RUSSIA	85.53	11.2%

...As the West Slows

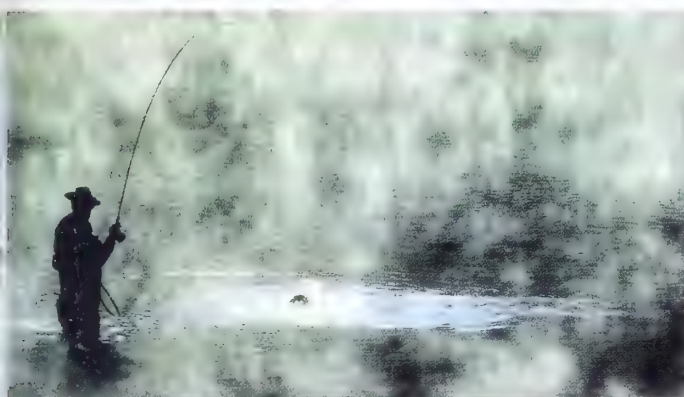
EUROPE**	3.81	23.3%
U.S.	3.7	40.7%

*Through 7/19/96 **European Composite
DATA DATASTREAM

end funds, such as the Czech Republic Fund, the safest most accessible means of entry is a diversified emerging markets fund. Robeco Stephens Developing Countries Fund, up 27% for the year, is more heavily weighted in Eastern European countries than most other offerings in its class. It also has one of the best returns among its peers year-to-date: 19.5%, according to Morningstar.

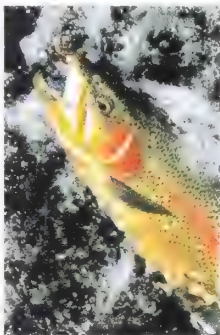
Remember, emerging markets are high risk, and you should only account for a small portion—5% to 10%—of your overall allocation of assets. That said, however, you're thinking about investing here, don't wait for "When you see unique opportunities opening up in this one, you have to go there," says Sheldon Jacobson, editor of *The No-Load Investor*. While it has taken years for the Eastern European countries to make the transition from communism to capitalism, the chance to buy into their markets at the bottom probably won't last long. *Kerry Coe*

Some nations of the old Soviet bloc are on a roll, exporting at a rate that has Western Europe jealous



WILD AND WILY TROUT— AND NOT IN MONTANA

fur dun, green
lake, blue-winged
e, quill Gordon,
olly bugger. To the
fishing eye they seem but
fluffs of hair wrapped
nd nasty little hooks,
ly deserving of
exotic names.
on the Upper
ware, howev-
expert hands,
e flies come to
as the highly
ed deceivers
are, luring
their barbs
of the wildest,
ingest, most
eous trout
where.
ry fly fishing—
re the fly is



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Tougher to fool

upon the surface to
at the trout—first took
in the U.S. on these cel-
ted Catskill waters, and
wonder. On a recent Sun-
morning, a bright sun
g behind our tents, I and
rusty fishing crony, Jim-
eased into the West
ch, near Deposit, N.Y.
ough the river was high
fast, we waded for hours,
ig no one, casting long
upstream, as we explored
ng the channels and the
ds. We caught just two
vn trout each, and not
big ones either. Howev-
two browns here are

worth eight anywhere else.

This is wild-trout country. When fly fishermen talk about smart, it's usually about the trout in their lives. And they're talking natives, trout born of eggs in such rivers as these, grown to size against disease and predators,

and a lot smarter for it. You can fool these trout onto your line, but you have to know the insects of the river as they hatch, and you have to cast the right fly just ahead of where you think you saw that trout rise last.

Miss and you may spook him. That makes these wild trout distinctly unlike most fished in America these days: the stocked ones raised in state hatcheries and dumped in local streams. They're bred pampered, not

HOOKED: Anglers often get addicted

smart, and they'll go chasing after everything—worms, lures, even gum wrappers—until they're fished out or die.

True wild-trout waters are scarce, especially near urban areas, and that's part of what makes the Upper Delaware unique. It's

two hours northwest of New York City, convenient to Philadelphia and even Boston. Yet fishing it, you would think you were in Montana.

The region spans hundreds of square miles and includes 100-plus miles of wide, fishable rivers. From Deposit, the West Branch flows south and east to

LEISURE

Hancock, N.Y., where it meets the East Branch, which has merged to the east with the famed Beaverkill, and the two branches together tumble into the Main Branch, flowing 75 miles to Port Jervis. The rivers remain cool, ideal for browns and rainbows through the hot summer months. Fishing remains good through the fall, and well-bundled diehards even fish in the winter.

BULKED UP. The fishing is always serious. The trout here have the brawn of their Western cousins, growing to 27 inches long on the Main Branch, but they're considered brainier, harder to catch, and certainly harder to keep on the line. "The Delaware River rainbow has equal stamina to any native-born

Western rainbow in Montana, Wyoming, and Colorado," says John Houghtaling, owner of Fly Fishing Plus in Riverdale, N.J. "They'll clean a reel in a second."

Jimbo and I fished on our own, but it makes sense for anyone new to the rivers to hire a guide, either for wading or floating in a drift boat. A guide will know what's hatching and what flies are working. A guided wading day for two runs \$225 at the West Branch Angler & Sportsman's Resort (607 467-5525) and the Delaware River Club (717 635-5880), the two best-known resorts. Float trips run a bit more.

NO LOOSE LIPS. Lodging is surprisingly cheap. The most expensive cabin at the West Branch Angler goes for \$300 a night, but it sleeps up to five.

We paid \$15 apiece to camp at a private grounds, but nearby there's Oquaga State Park at \$14 for up to six people, with hot-water showers, yet (800 456-CAMP). A handy listing of area motels, fly shops, and streamside resorts can be found in the *Mid-Atlantic Fly Fishing Guide*, available at fly shops from Virginia to Connecticut. Or try the Chambers of Commerce in Hancock (800 668-7624), Deposit (607 467-2556), or Livingston Manor (914 439-4859).

If you do come, though, don't tell a lot of people. Big as it is, old as it is, the Upper Delaware is still kind of a secret. Let the others go to Montana. We'd rather fish these legendary waters any day.

E.S. Ely

WORTH NOTING

■ **AIRLINE CAUSES.** United Airlines announced it will collect spare foreign change from passengers on flights between Chicago and London, then donate the money to the U.S. Committee for UNICEF. Why not? Most banks won't convert foreign coins, and just \$2 worth can provide enough Vitamin A to protect 60 toddlers from blindness. Meanwhile, Northwest Airlines will auction off vaca-

tion packages on Sept. 27 at Sotheby's in New York to benefit Habitat for Humanity International. The catch: You must bid with Northwest frequent-flier miles that you already possess or buy for 5¢ apiece.

■ **GOLF CHARGE.** American Express has launched a no-fee Optima card that lets golfers redeem points for equipment, greens fees, instruction, apparel, and advance tee times. Call 800 AXP-GOLF.

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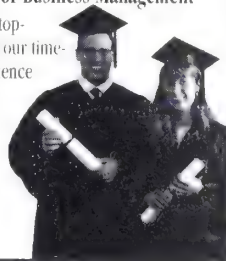
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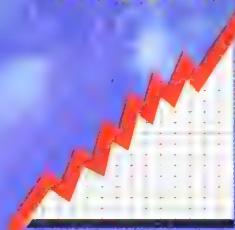
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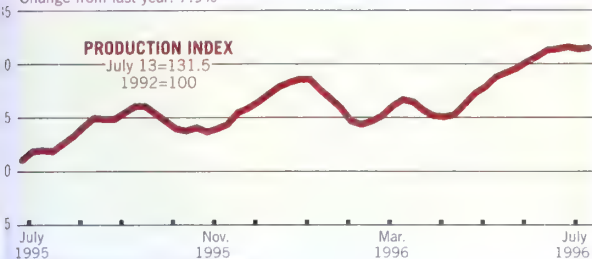


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Business Week Index

PRODUCTION INDEX

Change from last week: 0.1%
Change from last year: 7.9%



The production index edged higher in the week ended July 13. Before calculation of the four-week moving average, the index increased to 132 from 130.9 in the week before. After seasonal adjustment, production gains in autos, trucks, coal, lumber, and rail-freight traffic more than offset declines in steel, electric power, and crude-oil refining. Paper and paperboard production data were not available.

The leading index will be unavailable for an indefinite period.

*Production index copyright 1996 by The McGraw-Hill Companies

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (7/19) S&P 500	638.73	646.19	14.9
CORPORATE BOND YIELD, Aaa (7/19)	7.79%	7.89%	2.1
INDUSTRIAL MATERIALS PRICES (7/19)	106.3	106.2	1.6
BUSINESS FAILURES (7/12)	NA	NA	NA
REAL ESTATE LOANS (7/10) billions	\$521.8	\$521.7r	6.2
MONEY SUPPLY, M2 (7/8) billions	NA	NA	NA
INITIAL CLAIMS, UNEMPLOYMENT (7/6) thous.	370	351	-6.3

Sources: Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (7/23)	5.25%	5.20%	5.75%
COMMERCIAL PAPER (7/24) 3-month	5.50	5.55	5.80
CERTIFICATES OF DEPOSIT (7/24) 3-month	5.51	5.54	5.77
FIXED MORTGAGE (7/19) 30-year	8.44	8.55	7.95
ADJUSTABLE MORTGAGE (7/19) one-year	6.21	6.15	5.95
TIME (7/23)	8.25	8.25	8.75

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

EMPLOYMENT COST INDEX

Friday, July 30, 8:30 a.m. EDT ► Wage and benefit costs are expected to have risen 0.2% in the second quarter, according to economists surveyed by MMS International, of The McGraw-Hill Companies. The index rose 0.7% in the first quarter.

INGLE-FAMILY HOME SALES

Friday, July 30, 10 a.m. EDT ► June sales of new houses are projected to dip to an annual rate of 780,000, from 828,000 in May.

CONSUMER CONFIDENCE

Friday, July 30, 10 a.m. EDT ► Economists for the Conference Board's July index are expected to rise to 98.6, up from 97.6 in June.

GROSS DOMESTIC PRODUCT

Thursday, Aug. 1, 8:30 a.m. EDT ► Real GDP is expected to have grown at a 4% annual rate in the second quarter, up from 2.2% in the first quarter.

PURCHASING MANAGERS' INDEX

Thursday, Aug. 1, 10 a.m. EDT ► The nation's purchasing managers will report a rise in their July index of industrial activity, to 55%, up from 54.3% in June, the economists forecast.

CONSTRUCTION SPENDING

Thursday, Aug. 1, 10 a.m. EDT ► June construction outlays are expected to show a 0.5% gain, following a 0.9% drop in May.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (7/20) thous. of net tons	1,939	1,941#	3.9
AUTOS (7/20) units	123,199	46,859r#	26.1
TRUCKS (7/20) units	96,740	29,810r#	4.4
ELECTRIC POWER (7/20) millions of kilowatt-hrs	73,630	70,594#	0.4
CRUDE-OIL REFINING (7/20) thous. of bbl./day	14,141	14,147#	-1.6
COAL (7/13) thous. of net tons	18,045#	13,554	-6.1
PAPERBOARD (7/13) thous. of tons	872.9#	884.3r	-3.3
PAPER (7/13) thous. of tons	767.0#	771.0	-6.8
LUMBER (7/13) millions of ft.	457.2#	300.2	10.5
RAIL FREIGHT (7/13) billions of ton-miles	24.7#	21.3	0.0

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPAA, SFPAA, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (7/24) \$/troy oz.	384.400	383.400	-0.5
STEEL SCRAP (7/23) #1 heavy, \$/ton	133.50	133.50	-5.0
COPPER (7/20) ¢/lb.	91.3	93.7	-35.4
ALUMINUM (7/20) ¢/lb.	68.5	70.0	-23.9
COTTON (7/20) strict low middling 1-1/16 in., ¢/lb.	77.55	76.55	-15.2
OIL (7/23) \$/bbl.	21.67	22.24	26.7

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (7/24)	107.93	108.66	88.55
GERMAN MARK (7/24)	1.49	1.49	1.39
BRITISH POUND (7/24)	1.55	1.55	1.60
FRENCH FRANC (7/24)	5.03	5.03	4.79
ITALIAN LIRA (7/24)	1516.0	1522.0	1588.0
CANADIAN DOLLAR (7/24)	1.37	1.37	1.36
MEXICAN PESO (7/24)	7.608	7.648	6.100

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

LABOR MARKETS

Friday, Aug. 2, 8:30 a.m. EDT ► Nonfarm payrolls in July are projected to have increased by 200,000, after June's 239,000 gain. The jobless rate is expected to have edged up to 5.4%, from 5.3%.

PERSONAL INCOME

Friday, Aug. 2, 8:30 a.m. EDT ► Personal income in June probably jumped 0.9%, reflecting the month's surges in hourly earnings and the workweek.

FACTORY INVENTORIES

Friday, Aug. 2, 10 a.m. EDT ► Manufacturers' inventories were nearly flat in June, after a 0.2% dip in May.

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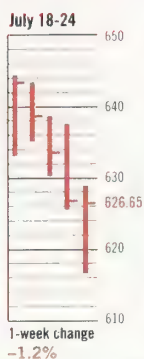
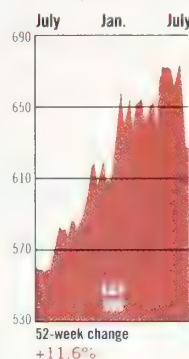
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Investment Figures of the Week

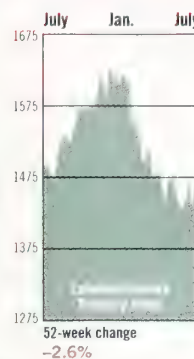
COMMENTARY

st in the U.S. stock market con-
ed, with small-cap stocks feel-
special pain as investors fret-
about earnings. The Nasdaq
posite index fell a jolting 3%
ily 23, declining to its lowest
in six months. Blue-chips
not spared, with the Dow
s industrial average falling
st 120 points in three days of
ng, from 5464 on July 18 to
on July 23. But the Dow
ad a small 8-point recovery on
24—after declining 76 points
ing the day—while broader
es kept falling.

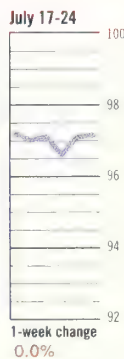
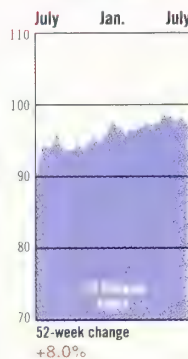
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
JONES INDUSTRIALS	5354.7	-0.4	13.8
IZE COMPANIES (S&P MidCap Index)	214.3	-2.7	4.5
L COMPANIES (Russell 2000)	307.8	-3.3	3.9
OMPANIES (Russell 3000)	353.9	-1.6	10.2

FOREIGN STOCKS	Latest	% change (local currency) Week	% change 52-week
ON (FINANCIAL TIMES 100)	3668.8	0.3	6.2
O (NIKKEI INDEX)	20,631.0	-3.7	25.9
NTQ (TSE COMPOSITE)	4880.3	-1.2	6.0

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.30%	5.26%	5.61%
30-YEAR TREASURY BOND YIELD	7.04%	7.03%	6.88%
S&P 500 DIVIDEND YIELD	2.29%	2.26%	2.38%
S&P 500 PRICE/EARNINGS RATIO	18.0	18.7	16.6

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	633.7	632.4	Negative
Stocks above 200-day moving average	40.0%	43.0%	Positive
Speculative sentiment: Put/call ratio	0.69	0.89	Neutral
Insider sentiment: Vickers sell/buy ratio	2.21	2.26	Neutral

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

MONTH LEADERS	% change 1-month	% change 12-month	Strongest stock in group	% change 1-month	% change 12-month	Price
LAND AND GAS DRILLING	8.6	67.7	ROWAN	10.5	117.2	15 ³ / ₄
EXPLORATION AND PRODUCTION	6.7	16.6	BURLINGTON RESOURCES	9.5	18.5	44 ³ / ₄
SMETICS	2.4	31.6	GILLETTE	8.3	48.7	63 ³ / ₄
NEY CENTER BANKS	1.1	32.6	BANKAMERICA	6.7	44.8	78
TURAL GAS	0.6	28.1	COLUMBIA GAS SYSTEM	10.6	52.6	52 ¹ / ₄

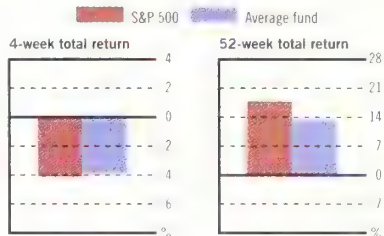
MONTH LAGGARDS	% change 1-month	% change 12-month	Weakest stock in group	% change 1-month	% change 12-month	Price
UCKING	-27.3	-37.0	CALIBER SYSTEM	-43.4	-53.3	19 ³ / ₄
CHINE TOOLS	-24.5	-34.9	GIDDINGS & LEWIS	-35.5	-30.5	11 ¹ / ₈
NG-DISTANCE TELECOMMUNICATIONS	-17.7	-0.8	AT&T	-20.1	-6.3	50 ¹ / ₄
OADCASTING	-17.2	-16.0	TELE-COMMUNICATIONS	-23.5	-20.7	14 ¹ / ₄
IOS	-17.1	5.8	UNITED HEALTHCARE	-31.3	-23.4	33 ¹ / ₂

MUTUAL FUNDS

MORNINGSTAR INC

LEADERS	Week total return	%	LAGGARDS	Four-week total return	%
DELITY SELECT NATURAL GAS	6.4		FIDELITY SELECT AIR TRANSPORTATION	-19.0	
ESCO STRATEGIC ENERGY	4.1		PREMIER STRATEGIC GROWTH	-14.2	
CELSIOR LONG-TERM SUPPLY OF ENERGY	4.0		RESERVE INFORMED INVESTORS GROWTH A	-12.9	

	Week total return	%		52-week total return	%
NDMARK SMALL CAP EQUITY A	77.3		STEADMAN TECHNOLOGY GROWTH	-31.8	
RNER SMALL CAP EQUITY	49.9		STEADMAN AMERICAN INDUSTRY	-24.7	
EMONT U.S. MICRO-CAP	48.1		SELIGMAN COMMUNICATIONS & INFORM. D	-21.5	



RELATIVE PORTFOLIOS

DRIAMCRAW HILL

Amounts represent the
net value of \$10,000
held one year ago
each portfolio

Percentages indicate
yearly total returns

U.S. stocks
\$11,414
-0.24%

Foreign stocks
\$10,838
+0.29%

Money market fund
\$10,529
+0.11%

Treasury bonds
\$10,479
+0.68%

Gold
\$10,231
+0.39%

Amounts on this page are as of market close Wednesday, July 24, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as

of market close July 23. Mutual fund returns are as of July 19. Relative portfolios are valued as of July 23. A more detailed explanation of this page is available on request. r=revised

GET BACK TO THE BUDGET, GUYS

The numbers certainly are impressive. The federal budget deficit, according to the Office of Management & Budget, will fall this fiscal year to \$117 billion, or about 1.6% of gross domestic product. The deficit as a share of GDP hasn't been that small since 1974. But it's way too early to cheer. Credit is due, OMB admits, mostly to higher tax collections resulting from a stronger-than-expected economy. And the deficit is slated to start climbing again in fiscal 1997—and could hit \$403 billion by 2006, according to estimates by the non-partisan Congressional Budget Office. That's thanks to runaway entitlement costs, chiefly Medicare, and mounting interest on the \$5.1 trillion debt.

Serious budget-cutting efforts have stalled in Washington, and now the Republicans are pushing for a massive income-tax cut (page 24). GOP supply-siders Jack Kemp and Steve Forbes, along with Senate Majority Leader Trent Lott (Miss.) and House Majority Leader Richard K. Armey (Tex.), are applying maximum pressure on presumed GOP Presidential nominee Bob Dole to focus his campaign on tax cuts. Dole appears to be caving in.

We went down this road before in the early 1980s, and look where it left us: battling budget deficits and paying that huge interest bill. Everyone favors tax relief—but it cannot come without commensurate spending cuts, as *BUSINESS WEEK* noted in its prescription for economic growth recently (BW—July 8). We cannot, as the supply-siders believe, simply grow ourselves out of the budgetary fix when we enact tax cuts without offsetting spending cuts.

The fact is that the hard work on the budget is yet to be done, and both parties have shunned the tough decisions of late. Clinton did manage, during his first term, to cut the deficit in half. But recently the Administration has simply carped about how the Republicans are "attacking" Medicare. It wasn't so long ago that the Republicans vowed in their Contract With America to bring the budget into balance. Now they're embracing massive tax cuts. It's time for both parties and their leaders to recognize that trouble lies ahead, and plans should be made to redouble budget-cutting efforts. We await the details.

MANDATE BOMB SCANNERS NOW

It's shocking but true: Since April, 1992, the TWA terminal at John F. Kennedy International Airport in New York has had equipment that scans luggage for drugs and could, with some slight modifications and minimum expense, be employed to detect explosives (page 76). But the machines are used by the U.S. Customs Service, not the airline,

therefore they inspect only luggage that is incoming.

Although the cause of the crash of TWA Flight 800 has yet to be determined, the threat of terrorist incidents looms large around the globe. Forty or so airports in Europe have already installed U.S.-made equipment to detect bombs, while numerous others have ordered the equipment. The European Civil Aviation Conference has stipulated that checked baggage must be electronically screened by 2000.

In the U.S., the Federal Aviation Administration has yet to mandate the use of such high-tech scanners, in part because it wants them to be almost totally automatic and not subject to human error. That's understandably driving costs higher and prolonging development. Today, the one system that would satisfy the FAA costs \$1 million. It is being used on a trial basis at only three airline terminals in the U.S.—two in Atlanta and one in San Francisco.

Instead of waiting for ideal solutions, the FAA should give the airlines the option of installing existing machines—some of which cost as little as \$125,000. And it should permit the airlines to keep that equipment even after it issues new final guidelines for such scanning equipment—so long as the airlines can show that their equipment is equally effective in spotting explosives. The key to their effective use, it turns out, is proper training of the machine operators. Yes, all this will raise the cost of doing business to the airlines, but yes, the public will have to pay for it in higher ticket prices. But edgy fliers might just be willing to ante up.

DON'T SELL THE SHORTS SHORT

Short-sellers don't get any respect. No surprise there. They can take one of Wall Street's darlings and smear its reputation in a jiffy with tales of financial intrigue and corporate malfeasance. Their dogged and persistent bad-mouth can drive corporate executives to distraction—and push stock prices to new lows. So when nervous executives and their guns on Wall Street orchestrate a short squeeze, the short-seller takes a drubbing (page 62).

These days, of course, the shorts are in their element: a down market, or even a jittery one, gives them a chance to say "I told you so." But it's not just this market that validates the contrarian view.

Consider how often short-sellers have been hounded by telling stories of accounting irregularities—only to be proven right several months down the road. Or how often they have correctly, if prematurely, pricked the balloon of overblown expectations for new products. To be sure, many short-sellers employ questionable tactics, and some have even engaged in prohibited activities such as selling short without borrowing the securities. But short-sellers are clearly outgunned when measured against the Wall Street elite's publicity machine, which almost always tells a bullish story. So here's a word to the wise investor: Keep an ear tuned to what the short-sellers have to say.

PROFITS SECOND-QUARTER RESULTS
FOR 900 COMPANIES

TAX CUT WILL IT DO MORE
HARM THAN GOOD?

ESS WEEK
August 12

BusinessWeek

AUGUST 12, 1996

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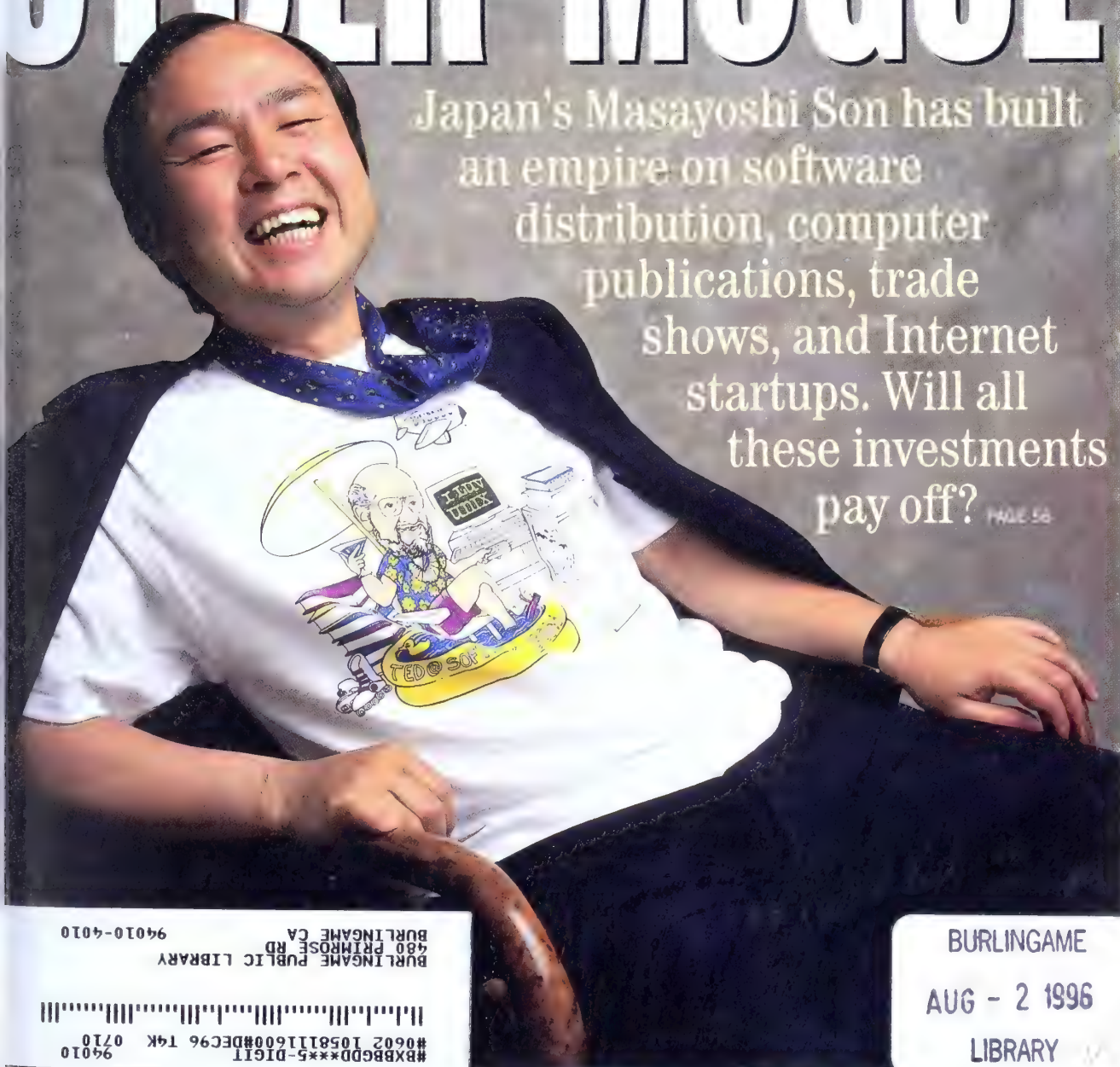
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CYBER-MOGUL

Japan's Masayoshi Son has built
an empire on software
distribution, computer
publications, trade
shows, and Internet
startups. Will all
these investments
pay off? PAGE 58



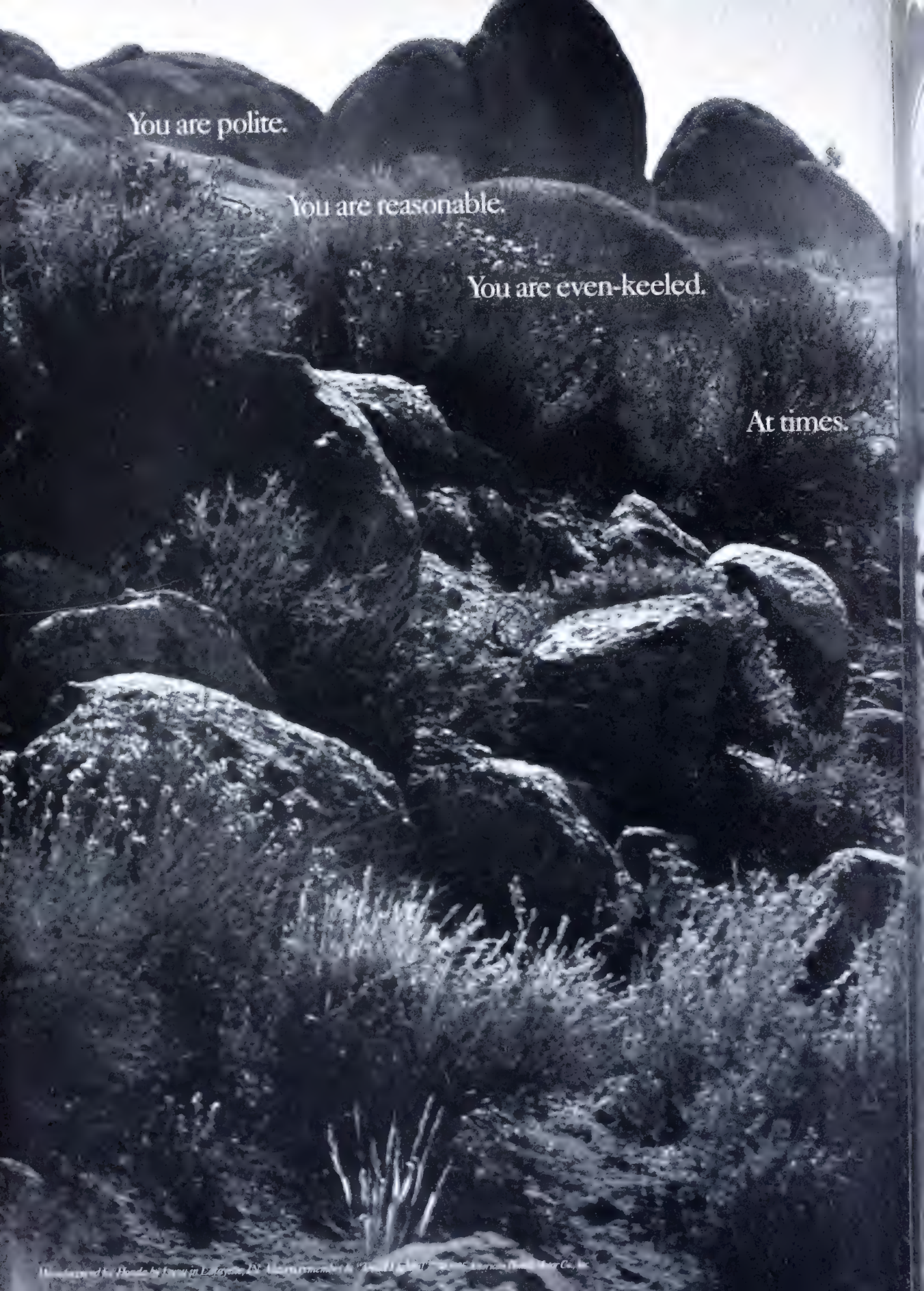
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BusinessWeek

AUGUST 12, 1996

COVER STORY

CYBER-MOGUL

Masayoshi Son has American business instincts, Japanese drive, and Korean roots. As for his dreams, they dwell in cyberspace *page 56*



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Softbank's Masayoshi Son has made it his life's work to ignore Japanese business conventions and earn a \$4.5 billion fortune before his 40th birthday. But the maverick entrepreneur's buying spree of information-technology assets has left Softbank \$2.4 billion in debt. So far, currency swings have worked in Son's favor, but cycles are fickle, and Son is balancing on the high wire as he tries to conquer the Net

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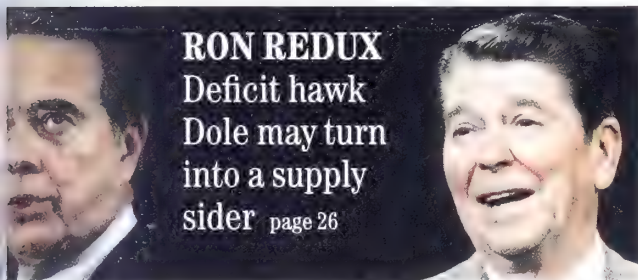


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Up Front

EDITED BY LARRY LIGHT

NEW WORLD ORDER

CUBA BOUND? SEE YOUR LAWYER

WASHINGTON HAS SPARKED an uproar by planning to penalize foreign companies doing business with seized U.S. property in Cuba. Less noticed: The feds are also coming down harder on U.S. violators of the 33-year-old embargo against Fidel Castro's regime.

Already this year, there have been 63 cases with civil penalties totaling \$489,727. That's more than all of 1995 (\$321,180, 53 cases). About two-thirds of the cases involve companies; the rest, individuals. This is an outgrowth of 1992 legislation tightening the embargo. BUSINESS WEEK filed a Freedom of Information Act

request for a full list of violators, but the feds say that will take many months due to backed-up requests.

Another factor in the crack-down is that more American businesspeople are interested in Cuba. The U.S.-Cuba Trade & Economic Council says the number of U.S. executives legally traveling there thus far this year exceeds 1995's 1,300. In 1994, only 400 went.

The feds do permit very limited Ameri-



formed an organization, hired a lawyer, and lodged fierce protests with HFS. So the parent company gave them back most of what they had had before. Remaining sore points include a 75% cut in Century 21's nationwide support staff and re-

SLUGFESTS

CENTURY 21'S HOUSE DIVIDED

HFS, THE HUGE REAL ESTATE company, is skirmishing with numerous franchisees of Century 21 Real Estate, which it bought a year ago for \$200 million from Met Life. Some brokers for Century 21, the nation's largest home-sales outfit, have rebelled over a recent HFS bid to charge more for franchises when they come up for renewal. And while HFS backed off, the resentment lingers over this and other simmering issues.

The fracas began when HFS tried to boost franchise renewal payments of about \$1,000 to \$25,000 or more, depending on a firm's market value. Plus, if a broker went out of business, he or she still would have had to pay corporate headquarters two years of annual franchise fees. And HFS doubled the franchise term to 10 years.

Dissident franchisees



NO CIGAR: El Presidente

TALK SHOW "Politics isn't a golf tournament. There's no prize for second or third or ninth place."

—GOP Chairman Haley Barbour, after denying Pat Buchanan a prime-time speech at the party convention.

can commercial activity if they license it. But some companies run afoul of the embargo's technical provisions. AT&T was fined \$12,700 in October, 1994, when gear for its long-distance telephone service to Cuba was shipped just days before receiving a U.S. license. AT&T it-

self reported this. Merck paid a \$127,500 fine last September after a visit to a Cuban biotech institute. Merck employees brought hepatitis B vaccine samples back for testing, which weren't permitted under Merck's license. *Gail DeGeorge and Stan Crock*

duced services to brokers. Yet the franchise fee—6% of yearly proceeds—is unchanged. And franchise renewals are no longer automatic, as they were under Met Life.

Now, some veterans, such as 23-year franchisee Joe Jannace of Hicksville, N.Y., are talking of not renewing with Century 21. An HFS spokesman insists that all the friction with franchisees is in the past. *Toddi Gutner and Nanette Byrnes*

BILL'S BUNCH

CHINA MUST SEEM LIKE A CAKEWALK

AFTER MUCH HEMMING and hawing, the White House finally decided to nominate Charlene Barshefsky as official U.S. Trade Representative. But the Administration is queasy about the appointment, and her fate rests with Senate Republicans.

Reason: a provision of a new ethics law, authored by Bob Dole, that bars Trade Reps who ever worked on behalf of a foreign government in a trade dispute. Barshefsky was a Washington lawyer for Canada. Her office says she merely monitored trade matters.

If the Republicans create a ruckus over her, Clintonites may end up pressuring Barshefsky to withdraw. Says a Democratic operative: "We go to the mat for someone who isn't a political player."

The White House's handling of Barshefsky has some officials grumbling about the shabby treatment of top-level women, such as Imelda Guinier, nominee manna, chief civil rights enforcer. "The Clinton boys are letting another girl twirl slowly in the wind," fumes a Clintonite. An official at the White House—which must act now on Barshefsky's 120-day interim term—up Aug. 8—insists she has its full backing.

Meanwhile, her uncertain status could undermine her U.S. in disputes with Japan (on insurance) and South Korea (on telecom). Already Tokyo officials have been talking about this. *Amy Bon-*



BARSHEFSKY: GOP target

THE LIST GOING THE DISTANCE

MCI Communications' attention to subscribers—it routinely checks in on them—makes the long-distance carrier the top choice in a customer-satisfaction survey of senior execs. Department-store chain Nordstrom, No. 2, is legendary for helping shoppers. Who's the worst? A huge majority in the survey name the U.S. Postal Service.

BEST CUSTOMER SERVICE

1. MCI
2. NORDSTROM
3. HOME DEPOT
4. AMERICAN EXPRESS
5. SATURN
5. LANDS' END
5. STARBUCKS

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Up Front

AFTERLIVES

PEROT'S RUNNING MATE TAKES A WALK

ROSS PEROT, NOW GEARING UP for another independent Presidential bid, has lost at least one supporter: his 1992 running mate, James Stockdale. The retired vice-admiral will be attending the Republican convention in San Diego as a California delegate backing Bob Dole.

Except for his Perot stint four years ago, Stockdale says he has always been a faithful Republican. Stockdale, whose stolid public style was ridiculed after the '92 Vice-Presidential debate, joined the Texas billionaire's ticket as a "personal favor to an old friend."

Stockdale says he's still a

good Perot pal. His allegiance to Dole stems from the 7½ years the former pilot spent as a prisoner of war in Vietnam. Senator Dole aided Stockdale's wife, Sybil, in her efforts as head of a group to free POWs.



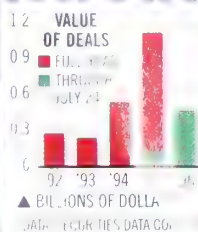
STOCKDALE: *This year, a Dole backer*

Soon after Perot lost, Stockdale returned to writing, lecturing, and studying his passion: philosophy, especially stoicism. Representative Sam Johnson (R-Tex.), a fellow POW, says that in the 1992 debate against Al Gore and Dan Quayle, Stockdale "should have popped Aristotle on them, and they wouldn't have known what hit them."

THE BIG PICTURE

GAMES FINANCIERS PLAY

Takeover players are raising a sweat in the sportswear and sporting goods arena. Warnaco Group's \$402 million bid for Authentic Fitness was recently scrapped. But such other deals as Brunswick's \$120 million buyout of Nelson/Weather Rite are making 1996 a strong year.

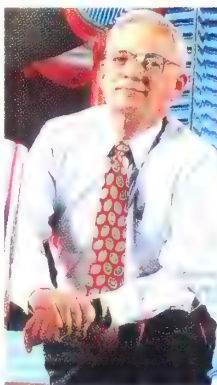


GADFLIES

A SISTER ACT ROCKS THE CORNER OFFICE

USUALLY, GADFLIES are lucky to get mike time at annual meetings. However, Sister Susan Mika, a Benedictine nun, actually has had an impact.

At Aluminum Co. of America's meeting last spring in Pittsburgh, she complained about wages and safety conditions at its Mexican plants. Chairman Paul O'Neill, a staunch safety advocate, later sat down with Mika and other labor activists. Then he dispatched a fact-finding team to the eight Mexican plants, which operate under an Alcoa joint venture with Fujikura, a Japanese electronics company. In May, O'Neill himself



O'NEILL: *Trouble in Mexican plant*

went to Mexico to have a look.

The chairman recently wrote to Alcoa execs that Mexico managers hadn't told headquarters of two 1994 carbon-monoxide poisoning incidents that temporarily affected 195 workers at the Ciudad Acuña auto-parts plant. The upshot: O'Neill dismissed the \$1.4 billion Mexican division's chief, Robert Barton. "It was a particularly painful decision for me," O'Neill wrote. He noted that Barton—who couldn't be reached for comment—had overseen huge growth in Mexican operations.

A triumph for Sister Mika, president of the Coalition for Justice in the Maquiladoras? "A good start," she says. Her organization is pushing Alcoa and others to lift wages above the current \$30-per-week average. *Stephen Baker*

DRAWN & QUARTERED



A guest lecturer at Stanford University's Hoover Institution think tank, Stockdale, 73, has just finished writing his third book, *Thoughts of a Philosophical Fighter Pilot*. Stockdale says that this collection of essays and speeches goes to "the core of what I believe to be true." Meanwhile, his nonacademic priorities include eight grandchildren and a daily swim. *Randi Feigenbaum*

BOOB TUBE

OUT OF THE LOOP IN SEATTLE



MICROSOFT HAS MOVED INTO cable television with MSNBC, but its employees can't tell channel surfing. All-nes MSNBC reaches 35% of cable-wired households, but the new Microsoft-NBC venture isn't available in Seattle or near Redmond, Microsoft's home.

TCI, which covers the Seattle area, says it lacks the channel space to carry MSNBC. TCI is now replacing its coaxial cables with higher-speed fiber, but that will take up to two years. Until then, Redmond just has 50 cable channels. Meanwhile, MSNBC hopes TCI will sub it for another service whose contract lapses. Other places MSNBC can't be seen include Dallas, Detroit, and Houston.

Busy Microsoft staffers can only view MSNBC at a few satellite-linked monitors in their lobbies and cafeterias. Says Redmond-based Microsoft Marketing Director Paul Boucaud: "I can't even see it at home." *Randi Feigenbaum*

There are a lot of questions you might ask a Nurse Case Manager.

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1. Act as advocates (see *ally*) for patients who require complex care, keeping them informed and involved in health care decisions.
2. Plan, assess and coordinate all health-related services.
3. Are one small part of a big idea called Informed Health™ (see *innovation*), a concept dedicated to keeping people better informed about their health and their care (see 1-800-AETNA-HC).



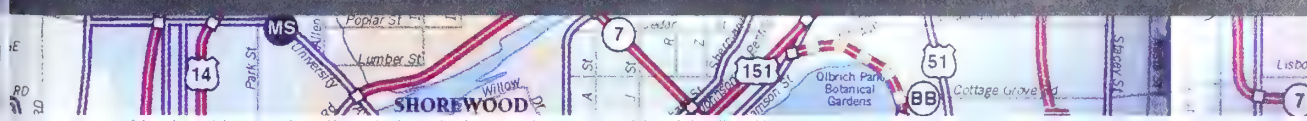
Informed Health from Aetna Health Plans

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TWO CHEERS FOR EMPLOYEE STOCK OPTIONS

In an age when the gains in stock prices and executive compensation consistently outpace gains in compensation for the average employee, it is encouraging to see such excellent coverage of a concept that addresses this disparity ("Options for everyone," Cover Story, July 22).

Many companies use broad-based stock-option plans because they know that employees are their most important asset and must be treated as such. For these companies, stock options are part of a visionary way of doing business: treating employees as true business partners and, as Robert Salwen notes in the article, creating "an environment that allows people to think and act like owners."

By realizing the dramatic effect that employee ownership and participation can have on corporate performance, companies such as Starbucks and Physician Sales & Service are emerging as leaders in their industries and expanding their workforces in the process. This is the true power of stock options or any other broad-based employee ownership plan.

Edward J. Carberry
Director of Communications
National Center for
Employee Ownership
Oakland, Calif.

What would that old visiting Marxist history prof I had back in college say if he could read all the articles I see nowadays about employees buying stock and getting stock options in their companies? Indeed, it's an idea whose time has come. The Soviet Union tried in vain for decades to get Russian workers to take ownership of their companies and see their efforts directly affecting their lives.

Now, in America, this trend of employee stock plans is taking hold more broadly. Employees are literally taking ownership of their companies and getting their own fiscal futures into

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shape. All this without political rick-
ness, bloody revolution, and decade of
wasted effort.

Matt Campbell
Philadelphia

THE LILAC BALL IS NOT THE PREDATORS' BALL

As chairman of the board of trustees of Prep for Prep, I call your attention to the comparison of the Prep for Prep Lilac Ball with the so-called Predators' Ball ("Drexel is dead. Long live the Drexel network," *Finance*, July 29). The statement in the article that the Lilac Ball is the Predators' Ball redux is without any factual basis, highly misleading, and very damaging to Prep for Prep. The Prep for Prep Lilac Ball has no relationship to the Predators' Ball.

As an officer and trustee of Prep Prep, Leon Black has made an enormous contribution to our organization and to the community. Through his generosity, dedication, and hard work, the 1996 Lilac Ball raised \$3 million—more than half the Prep for Prep budget. In addition, Leon Black has devoted much time and effort to the work of Prep for Prep. He joined the board of trustees at my invitation and has been a major factor in the success of Prep for Prep. Leon Black is a successful businessman, a devoted husband and father, a tireless worker for community betterment, and an outstanding citizen. Black needs no apologies or corrections.

Prep for Prep was misused in the article, and the record should be corrected.

Martin Lin
New

TAKING AIM AT SOCIAL SECURITY

Kudos to Paul Craig Roberts for sticking to his guns and telling it like it is in "Call me a jerk, but Social Security must be reformed" (Economic Viewpoint, July 22). I am 28, and every time I look at my pay stub and see the money I am throwing away on the intergenerational wealth-transfer sys-

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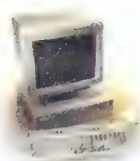
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wn as Social Security, I shudder to k what that money could be worth) or 30 years if it were invested in a dard & Poor's 500-stock index fund, ivate 401(k), or a similar retirement unt. Perhaps a better understanding ie facts, as you describe them, may : future generations a chance. nks, Paul, for a voice of reason.

Todd Breslow
Philadelphia

he simple truth about Social Securi- s that it is going to be reformed. way or another, it has to be re- ed. The question is how and when. we wait until the system collapses, o we act now, prudently, to ensure the promises made can be kept? ed on history, I am afraid that dis- r will have to strike. I hope, on the r hand, that sensible, rational people prevail and that some mixture of atizing and tax support for a floor efit can be realized.

he same people raising the warn- of bad investment decisions for a atized Social Security system seem ave no problem with the 401(k). I ider why? Could it be that the spe- interests and their amen chorus in federal bureaucracy don't feel atened by that, as they do with the on that Social Security could head in same direction?

laud your willingness to broach this ie and bring the simple facts to the ention of the public. Someone has to it. It's a pity it has become such an otional and thankless job.

Geoffrey K. Wascher
Utica, Mich.

NBC: DOES THAT STAND FOR IRE OF THE SAME NBC?

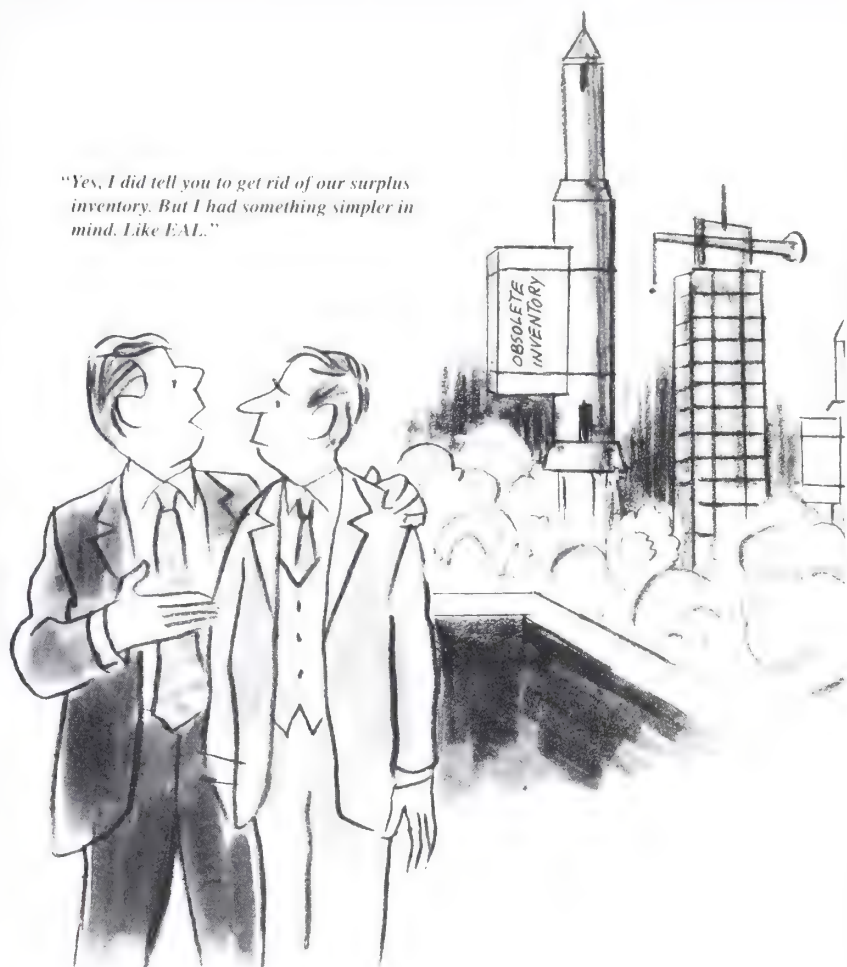
read with great interest and ex- ment your story about a new cable- vs network: MSNBC ("Network meets t," Cover Story, July 15). How re- shing to have a news program with v faces, perspectives, and ideas. Then I read that MSNBC will offer rs such as Tom Brokaw, Katie Couric, ie Pauley, Bryant Gumbel, and Bill yers. This sounds like the same old ne-old. Count this viewer out.

Rick W. Miller
Valparaiso, Ind.

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Readers Report

tap water with chlorine," as Greenberg says. Even if most microorganisms in the drinking-water supply are captured on filters and irradiated, subsequent chlorination is required to ensure the water's purity as it moves through the distribution system to the tap. No other water disinfection method alone—other than chlorine—provides this kind of residual protection from the regrowth of disease-causing microorganisms once the water leaves the treatment plant.

C. T. Howlett
Vice-President & Managing Director
Chlorine Chemistry Council
Arlington, Va.

OPENING UP SAUDI ARABIA— TO ISLAMIC ZEALOTS?

I am afraid that by suggesting the opening of Saudi Arabia's political system, we are doing precisely the wrong thing ("Don't let Saudi Arabia become another Iran," International Business, July 15). It has been said that "those who refuse to learn from history are doomed to repeat it." We encouraged the Shah of Iran to allow more freedom, which in turn allowed Khomeini to gain a foothold and seize control of

the country. The threat of Islamic fundamentalism extends beyond the Middle East. It is not just anti-American; it is opposed to any nonbelievers. We must become less reliant on Middle East oil. We cannot compromise with or debate radicals and zealots committed to gaining power by any means.

Paul S. Polkowski
Sunnyvale, Calif.

RUSSIA'S VOTE WAS NO THUMBS-UP FOR REFORM

The recent presidential election in Russia was not, as so many like to believe, a victory for democracy ("The new troika in Moscow," International Business, July 22). Nor was it, regrettably, an endorsement of reform. The election reflected a poor choice between an unsatisfactory status quo and the nightmarish specter of a return to communism—albeit restyled communism.

As for the description of Russia's new leaders as a "troika," we should really be talking about a new odd couple—namely President Boris Yeltsin and National Security Chief Alexander Lebed. Prime Minister Viktor Chernomyrdin does not have much of a power base in

his own right, but Lebed does. While the reelection of Yeltsin is exactly what the West wanted, we must not succumb to the false assumption that the reform process in Russia is alive and kicking.

Karl H. Page
London

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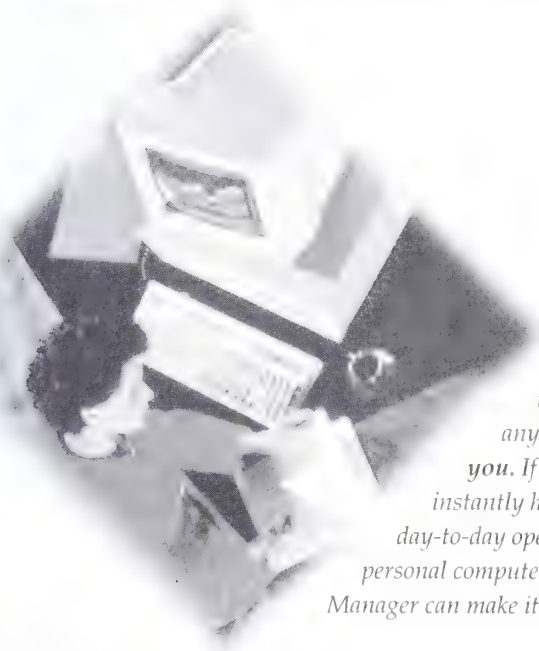
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SCIENCE ON TRIAL

The Clash of Medical Evidence and the Law in the Breast Implant Case

Marcia Angell, M.D.

W. W. Norton • 256pp • \$27.50

TRAMPLING SCIENCE IN A RUSH TO JUDGMENT

About a year ago, I started receiving mailings from Dow Corning Corp., one of the primary manufacturers of breast implants and the target of hundreds of thousands of lawsuits from women who have gotten them. Unsurprisingly, the clippings contained articles that denied any connection between breast implants and the terrible diseases they were accused of causing. At first, I shrugged the material off as company propaganda. But it wasn't much later that scientific articles and a wave of news reports led me to begin to question the accusations being made against implants.

Dr. Marcia Angell, the author of *Science on Trial*, began her questioning back in 1992. That's when Dr. David A. Kessler, head of the Food & Drug Administration, banned breast implants—ostensibly because there was not enough scientific evidence to prove they were safe. He submitted an article to the *New England Journal of Medicine*—where Angell is executive editor—outlining his reasons for the ban. After reviewing the manuscript, Angell realized that politics, public opinion, and the law played as great a role in Kessler's decision as science. Then, in 1994, just weeks after besieged implant manufacturers, including Dow Corning, had agreed to set aside \$4.2 billion to meet the claims of women with breast implants, doctors from the Mayo Clinic submitted the first epidemiological study to the journal finding no link between implants and connective-tissue disease.

In *Science on Trial*, Angell tells a tale that is becoming increasingly familiar. Fearing that new technology, ranging from medical devices to cellular phones, may be inherently harmful, the public and courts are quick to find fault without waiting for scientific evidence. With breast implants, courts awarded multimillion-dollar judgments based on

heart-rending anecdotes, unsubstantiated theories, and debatable expert opinion. But the scientific studies were nowhere to be found.

The cost of these actions is staggering. Implant manufacturers have spent hundreds of millions on claims so far. Dow Corning—an international supplier of silicone adhesives and other products, where implants made up just 1% of the business—filed for bankruptcy. At this point, the settlement is in a shambles as a result of that bankruptcy.

Angell's book highlights the dissonance between the culture of science and that of the legal world. Perhaps the biggest problem with science in the courtroom, according to Angell, is that it cannot provide absolutes. In the case of breast implants, for example, the Mayo Clinic study set out to test the hypothesis that implants increase the risk of connective-tissue disease. But researchers "could not find an association between implants and the diseases and symptoms they studied. If they had said that implants do not cause connective-tissue disease, they would have gone beyond what their data could support. The study did not rule out a connection."

In science, as more and more studies back up a hypothesis, it becomes accepted as a powerful or even reigning theory—but rarely as undeniable fact. (The connection between smoking and cancer is regarded as nearly incontrovertible—but only after 30 years of painstaking research.) In the hands of an adroit lawyer, however, such scientific caution is forgotten, as theories become powerful arguments for causation. Some so-called expert witnesses steamroll over complex scientific evidence—instead

spinning theories that they say are supported by their experience or unspecified research. In reality, these experiences often do not have relevant experience, says Angell, and their research may be unpublished or out of the mainstream. "The result," she writes, "is a growing gap between scientific reality and what passes for it in the courtroom."

The public is quick to believe courtroom explanations in the case of implants, argues Angell, because of growing anti-science sentiment in the U.S., a topic to which she devotes a chapter in the book. Coming in for particular scrutiny are "anti-science feminists" who embrace the idea that implants are deadly and, according to the writer, dismiss value-free research as a delusion fostered by a male-dominated profession that ignores "intuitive, multi-faceted thinking." As a result, these feminists, as well as the people who have given in to speculation and mysticism, "... could believe that implants caused disease because they 'knew' it."

Other chapters are devoted to the history of breast implants, a primer on scientific evidence, and an illuminating look at who is profiting from breast-implant litigation: a suspicious group of doctors, expert witnesses, and inevitably lawyers, Angell argues. At times, she is too strident in her defense of scientific method: A "reliance on concrete evidence distinguishes science from all other human endeavors," she writes. But given that she is an editor at a premier scientific journal, this can be forgiven. And *Science on Trial* is extremely well-documented, even though, at times, Angell relies heavily on press reports—especially from *The New York Times*—instead of original research.

Science on Trial is an important book that makes a strong case for bringing well-documented science into the courtroom as the best deterrent against such legal circuses as the breast-implant controversy or looming cases involving a variety of medical-device makers. Has a look, counselor.

BY NAOMI FREUNDLICH

Freundlich is BUSINESS WEEK's Science Editor.



IN BREAST-IMPLANT CASES, HUGE DAMAGES WERE AWARDED BEFORE STUDIES WERE COMPLETED

CATHERINE ARNST

TRIUMPH OF THE POWER PHONE

ny features can p you create an ce switchboard ht at home

all it a blessing. Call it a curse. But we have come to depend on -powered phone systems i voice mail and all the mings. Whether our child is a ride home from ce class or a client is ly to close a deal, we t to get our calls. The er phone is particularly cal for the growing ons of people who k from home and le some 100 calls a with no secretary. hese days your phone pany is fast becom- your secretary. Such ices as call waiting, e mail, call forward- and three-way call- have been available very state for a few s now, for about \$5 \$10 each per month. these bells and whis- fell short of turning a ie phone into a fac- le of the multifeatured of- switchboard because they dn't be combined. That's nging now.

BROADCAST TIME. Suppose, for example, you want to ek each incoming call to de whether to answer it send it to voice mail. You start by investing in a ne outfitted with a liquid- stal display, at a cost of to \$250. It will let you into the array of services t local phone companies programming into their tral switching offices. Be- s allowing residential cus-

tomers to make conference calls or selectively answer calls, the systems will let you send voice messages to many people at the same time. And your long-distance carrier is just as eager to offer fancy features—the most common is a personal phone number that will automatically ring you at whatever number you want it to.

Nynex' Call Manager is typical of the kinds of products available across the country. The service, which costs \$19 a month in New



York State, displays the phone number and name of an incoming call on a screen phone and allows you to deal with it in four different ways: You can forward the call to your voice mailbox, "conference" it in with the call you're already on, place the first call on hold and answer the second, or route it to one of two voice prompts—"Hold On" or "Call Back." Also, most regions allow the customer to program up to five different personal mailboxes so that a caller can choose to leave a message for you, your

co-worker—or one of your three teenagers.

Then, there's voice-mail broadcasting. Bell Atlantic just rolled out a service in Maryland, Virginia, and Washington, D.C., called T-Mail, which allows customers to use their voice mail to send the same message to another individual or to an entire group, all with one phone call. People can send, reply to, and copy messages to anyone within their regional calling area who also has a Bell Atlantic voice mailbox. Small businesses in particular can benefit. For example, the local hardware store could use T-Mail to alert its customers instantly to sales events. With prices starting at 15¢ per call, the cost can be less than the postage alone for flyers.

Most of the nation's local phone companies are plan-

tures, turn to your long-distance provider. They're the ones offering follow-you-anywhere phone numbers. Local carriers are not yet allowed to sell long-distance service.

KEEPING TABS. All the major carriers offer a service similar to AT&T True Connections, which assigns subscribers a 500 number that they can give to their clients and colleagues. When you leave home for a trip, you can program the 500 number to ring at a particular location. If you don't know where you're going, you can have calls ring automatically at up to three numbers—your home, cell phone, and pager, say, until you pick up. AT&T has been offering a series of promotions on True Connections: Right now, you can get the service for six months with no installation or monthly fee. Usually, it costs \$2.95 to \$4.95

A Sampler

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Combines caller I.D., call waiting, and other services. Allows you to see an incoming call's phone number on your screen phone and either forward it to voice mail or answer it while placing another call on hold. Cost: \$129 for the screen phone plus \$19 per month*

*In New York State. Prices vary by state

AT&T TRUE CONNECTIONS SERVICE

A 500 number that follows you wherever you go. Allows you to direct incoming 500 calls to up to three different numbers at a time until you pick up, or forward them to voice mail. It can also be used to charge calls. Cost: \$2.95 per month plus usage charges

a month, plus usage charges.

Down the road, phone companies are hoping to come up with a way to combine voice mail and E-mail delivery. "I would say it's a very high priority for everyone in the industry to develop a PC-compatible service," says Tim Munoz, managing director of Nynex' consumer markets. He thinks there will be integrated voice mail/E-mail sometime in the second half of next year. With that kind of service, you may never have to talk to anyone in person again.

ning, or have already started, to roll out a similar service. But you can only send a message to a voice mailbox in your immediate area because few central-office-based systems are compatible with each other. Phone companies, however, want to correct that drawback, and recently Ameritech, Bell Atlantic, Nynex, and Pacific Telesis banded together to develop mailbox-to-mailbox standards so customers won't have to know or care who uses which carrier's service.

For other fancy calling fea-

BY ROBERT KUTTNER

THERE MAY BE NO CURE FOR TAX-CUT FEVER



CONTAGIOUS:
Republican
supply siders
are pressuring
Dole into
offering a tax
cut—which
could spur
Clinton's camp
into delivering
its own version

Bob Dole and Bill Clinton have fallen into disfavor with large numbers of their own partisans for selling out the souls of their respective parties. Perhaps more than in any recent election, Republicans and Democrats will hold their noses this year as they vote for their party's standard-bearer. Clinton? He's barely better than Dole. Dole? He's almost as bad as Clinton.

To the Democratic faithful, Clinton has given away much of what the party stands for in his zeal to show that he, too, can balance the budget, shrink activist government, and be tough on social issues. The President's strategist, sometime-Republican Dick Morris, seems to be running not just the campaign but the Presidency. Furthermore, imitating the Republicans is apparently good politics: Clinton is way ahead of Dole.

OPPORTUNISM. For conservative militants, 16 years into the Reagan era and nearly two years into the Gingrich Congress the GOP nominee appears to be an ideological Rip Van Winkle who slept through the revolution. He likes fiscal probity more than tax reduction, religious moderates more than Christian fundamentalists, is soft on abortion rights, and he can't keep his lines straight. Even worse, Dole's moderation is bad politics. Somehow Clinton is able to make Republican themes work better than Dole does. Unlike Clinton, Dole gets no credit for his moderation. He's 20 points down in the polls. You can almost hear activists from opposite ends of the spectrum commiserating.

Now comes a big issue that could inject some ideological clarity—or new depths of bipartisan opportunism—into this dismal tableau: the call from the Republican right for yet another tax cut. It now appears that Dole will embrace a large and expensive tax cut. Dole's advisers have drafted a 15%, across-the-board cut, which would cost the Treasury about \$600 billion over six years.

Until now, Dole has called for a "flatter and fairer" tax system, but he resisted either a Forbes-style flat tax or the kind of sweeping tax cuts associated with Kemp, Gingrich, and Reagan. And with good reason. For more than a decade, as Senate Republican leader, Dole's job was to clean up after supply-side excess. In 1982, after the unsustainable cuts of the 1981 tax act, Dole joined the bipartisan effort to reduce the deficit, including some tax increases. He was also par-

ty to the deficit reduction deal of 1990, which raised taxes.

As Dole well knows, the progress toward a balanced budget by 2002 would be wrecked by major new tax reductions. As it is, both parties have conspired in the fiction that the unnamed program cuts deferred to 2001 and 2002 can make the numbers work. To reconcile tax cuts and budget balance, Republican supply siders would have to claim growth rates that would make Rosy Scenario blush (and Alan Greenspan tighten). Rising deficits, of course, would lead to higher interest rates, which would wreck the promised growth.

But what makes the promise of a tax cut virtually irresistible is not the economics, but the politics. Pollsters from both parties insist that a tax cut has immense voter appeal. With the Fed holding down growth rates and median earnings fairly flat, and with fiscal policy and program spending both tight, a tax cut is evidently the one activist thing that government can offer to put money in voters' pockets. And with Dole's campaign comatose and the party's militants in a depression, a call for major tax relief could ignite both GOP activists and voter enthusiasts. (Commentators and mainstream economists would surely denounce the ploy as irresponsible opportunism, but who cares about them?) Expect Dole to wrestle with his conscience, and lose.

CHRONIC DEFICITS. Speaking of opportunism, don't expect Dick Morris to take a new Republican tax cut lying down. Ever since Walter Mondale in 1984 tried to take the fiscal high road, pledging a tax increase in his acceptance speech, Democrats have found budgetary honor to be awkward politics. Clinton did the right thing with his 1993 tax increase aimed at the richest 2%, but congressional Democrats paid the price. In all likelihood the White House would unveil its own tax plan tilted more to the middle class rather than upscale voters—and offering the usual catchwords. Both parties would collude once more in the claim that we can afford lower taxes and still have budget balance.

A 1981-style bidding war to cut taxes would be bad for both economy and politics, would lead back to a politics of chronic deficits and permanent pressure to ratchet back public services. Even worse, it would again bestow on the likes of Ross Perot an improbable mantle of fiscal rectitude.

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THE NEXT G

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Can someone turn
the thermostat down?*



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BY GENE KORETZ

THE BOONIES BOOM, AT LAST

Lower taxes and wages fuel growth

After booming in the 1970s and tanking in the 1980s, rural America is making a startling comeback. A recent study by economists Mark S. Henry of Clemson University and Mark R. Drabenstott of the Federal Reserve Bank of Kansas City notes that rural employment growth in the 1990s has far outpaced job growth in urban areas (chart). And new research by demog-

raphers Kenneth M. Johnson of Loyola University in Chicago and Calvin Beale of the Agriculture Dept. finds that population growth has taken off as well.

“Not only are most rural counties adding residents,” says Johnson, “but a net outflow of 1.4 million people in the 1980s has already been offset by an inflow of 1.6 million people in the 1990s.”

One factor that seems to be fueling the rural influx is the general aging of the population. Counties offering retirement and recreational amenities have grown the most in recent years, a likely reflection of rising travel and recreation outlays by middle-aged baby boomers, and of the growing ranks of retirees.

Another plus has been proximity to metropolitan areas. Henry and Drabenstott report that in the past dozen years or so, many rural counties near metropolitan areas have actually posted faster nonfarm job growth than neighboring urban centers. Indeed, rural counties appear to have increased their share of the nation's manufacturing employment.

Still, the two economists found that the biggest rural job gains derived from what they called “industry clustering,” the ability of rural areas to build on the expertise of established local indus-

tries by developing similar activities. Industry clusters run the gamut from Sunbelt recreational areas and Oregon's “silicon forest” to carpet manufacturing in northern Georgia and catfish processing in the Mississippi delta.

One problem with the rural economic revival, notes Henry, is that employment growth has tended to involve relatively low-wage positions. Whereas many jobs created in urban and suburban areas pay above-average wages, jobs in rural areas have been concentrated at the lower end of the pay scale.

But lower labor costs, says economist Mark Zandi of Regional Financial Associates Inc., are a major factor behind the rural renaissance. The economic imperative today for both business and consumers is cost-reduction.

Aided by new communications technologies, companies find they can take advantage of the lower taxes, utility bills, and labor costs offered by rural areas. Consumers find living costs and taxes are lower, and quality of life—less pollution, crime, and congestion—is higher, so they're willing to accept lower wages.

It's a combination, says Zandi, that “should keep rural America growing for a long time to come.”

While protectionists may say “I told you so,” the declining ratio is good news for the economy as a whole, says Davis. The downward trend mainly reflects rising productivity gains and the ability of U.S. goods exports to command higher prices on world markets. And gains still look strong when services are factored into the equation. In 1995, exports of goods and services supported a record 11 million U.S. jobs—more than 10% of total employment—up from 6.3 million in 1986.

By Amy Borrus in Washington

ESTONIA: OPEN FOR BUSINESS
It has embraced the free market

Estonia is a tiny nation, with only 1.15 million people. Yet in its 15 years of independence, the former Soviet Republic has achieved a remarkable economic transformation.

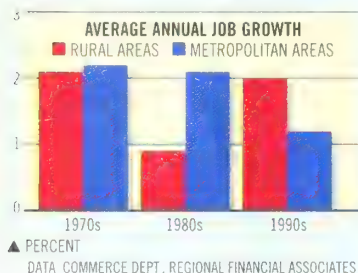
As economist David Hale of Zurich Kemper Investments Inc. notes in a recent commentary, economic output dropped by more than 40% in Estonia's initial years of independence, and inflation soared above 1,000%. But growth turned positive in 1995 and should hit 4% or 5% this year. Unemployment is only 5%, and inflation is close to 20% and falling.

Behind this progress lies a rapid shift of resources from inefficient industrial sectors to services and the adoption of market-oriented economic policies.

Estonia has no tariffs, no government deficit, a flat income-tax rate of 26%, and government outlays equal just 27% of gross domestic product. As in Hong Kong, monetary policies conducted through a currency board in this case, making the kroon convertible into the German mark at a fixed rate.

While much of Estonia's recent growth stems from its proximity to Finland (a 6-hour by hydrofoil) and its ability to attract nearly 3 million Finnish tourists a year, Hale notes that its capital, Tallinn, has one of the best harbors on the Baltic Sea. If Estonia can patch up its differences with Russia, he thinks it could become a major distribution center for eastern Russia and other neighbors—a veritable Hong Kong of the Baltic.

RURAL AMERICA'S EMPLOYMENT REVIVAL



HOW EXPORTS CREATE JOBS

An old rule of thumb is updated

It has become the mantra of free-traders: \$1 billion worth of merchandise exports supports 20,000 U.S. jobs. Ever since government officials trumpeted the numbers back in the Bush Administration, free-trade advocates have bandied about this ratio to justify efforts to open markets abroad.

Trouble is, the jobs number is way out of date. In fact, the exports-employment ratio has been falling steadily since the Commerce Dept. began measuring it in the early 1980s. The agency now estimates that in 1995, the average number of jobs supported by every \$1 billion worth of goods exports was 14,200, with the numbers varying widely by industry.

That's no surprise to Commerce's green-eyeshade brigade, long irked that the average for one year is freely used as a rule of thumb. “This is not an immutable ratio,” says Lester A. Davis, Commerce's senior international economist. “We've been discouraging people from using it since 1981.”

While protectionists may say “I told you so,” the declining ratio is good news

A BALTIC HONG KONG?



JAMES C. COOPER & KATHLEEN MADIGAN

THIS SHOPPING SPREE ISN'T OVER YET

U.S. ECONOMY As consumers go, so goes the economy. The old truism is part on forecasting power but long on explaining why the economy has been so surprisingly strong this year. With consumer confidence starting the second half on a six-year high, households still seem raring to spend, even amid higher borrowing costs and rising debts. The continued resilience of consumers, who buy two-thirds of gross domestic product each quarter, is a big reason why overall demand held up so well in the second quarter. And that strength has taken inventories down to levels that are causing increased ordering and output, adding momentum to the current quarter. You can also give consumers a nod for the unexpectedly solid performance of corporate profits last quarter (page 88). In fact, despite Wall Street's jitters, 57% of the more than 400 earnings reports announced through July 30 have been on the high side of expectations, according to Zacks Investment Research. Only 30% have been negative surprises.

HOUSEHOLD OPTIMISM HITS A SIX-YEAR HIGH



Against that backdrop, it's easy to see why consumers are not yet in a stew over their finances. If the markets suddenly turn soft, then households are likely to start thinking more about paying their bills and less about buying that new dishwasher. But that doesn't seem likely to happen anytime soon.

HOUSEHOLDS WERE AS OPTIMISTIC in July as they were back in May, 1990, near the end of the consumer boom of the late 1980s. The Conference Board's index of consumer confidence surged seven points last month, to 107.2, from June's reading of 100.1, which was revised up from the original report (chart). The board said that consumers' assessments of present conditions and expectations for the future both improved strongly. The driving factor in these upbeat appraisals appeared to be jobs and incomes. The number

of people who felt that jobs were "hard to get" fell in July, and those who described jobs as "plentiful" outnumbered those saying they were "hard to get" for the fourth month in a row, a break from the opposite trend earlier in the year.

The jump in the Conference Board's index matched the buoyant July readings seen in the University of Michigan's consumer sentiment index and the weekly ABC/Money magazine index. While the confidence indexes do not always foreshadow spending trends, the recent pattern does strongly suggest that the same factors that supported spending in the first half are still in place at the start of the second half.

ONE OF THOSE SUPPORTS is income growth, which has been strong not only because it's easier to find a job, but also because jobs are paying more. However, employers are offsetting the impact of faster wage growth in their costs by holding back on the size of benefits packages (chart).

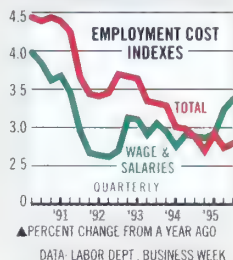
That much was clear from the Labor Dept.'s report on second-quarter employment costs. The employment cost index, which covers workers' compensation derived from both wages and benefits, is a broader and more reliable measure of labor costs than the monthly measure of average hourly earnings. It includes almost all payroll jobs, and it is a fixed-weight index that is not affected by the changing mix of jobs.

The growth of total compensation picked up a bit in the first two quarters of 1996, reflecting a sharp speedup in wage growth. The ECI rose 0.8% last quarter, and the first-quarter advance was revised up, also to 0.8%, from 0.7%. In the first half, the ECI rose at a 3.2% annual rate, vs. a 2.7% pace for all of 1995.

Wages and salaries grew 1% and 0.9% in the first and second quarters, respectively. That amounts to a 3.7% annual rate—the fastest two-quarter advance in five years and well ahead of inflation. That pace is certain to get the attention of the Federal Reserve's policymakers as they sit down later this month to decide what to do about interest rates.

However, the slowdown in the growth of benefits, such as health insurance, retirement plans, and lump-sum bonuses, as well as legally mandated programs such as Social Security, is holding down the overall

WAGES SPEED UP, BUT TOTAL COSTS DON'T



Business Outlook

growth of labor costs and moderating potential inflationary pressures. Benefits costs, about 30% of total compensation, rose 0.7% in the second quarter, after no increase in the first.

Overall benefits have grown only 1.8% during the past year, and the annual pace has been declining steadily for the past six years, from a high of more than 7% per year in 1990. Health care is leading the slowdown. Health-care costs in 1995 rose the least in 23 years, as managed-care programs forced pricing discipline among providers.

GIVEN SOLID INCOME GROWTH and an improving job outlook, it's no wonder home buying held up so well in the first half amid rising mortgage rates. Also, consumers are turning increasingly to cheaper variable-rate loans to cope with the rise in fixed-rate mortgages, where 30-year rates averaged 8.4% in late July.

Sales of both new and existing single-family homes declined in June, but not by much. New-home sales fell 5.3%, to an annual rate of 734,000, but sales had risen in both April and May (chart). For the quarter, new-home demand stood slightly ahead of the first-quarter level. Existing-home sales last quarter were sharply above their first-quarter level.

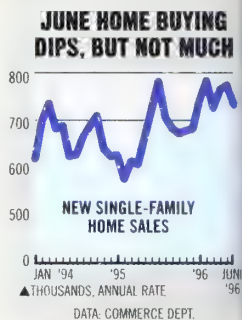
Still, because of the backup in mortgage rates, home buying probably peaked in the second quarter, but demand seems likely to remain at a high level. Nothing on

the horizon suggests a big downturn. In fact, mortgage applications to buy a home in mid-July were in the range that they have occupied all year.

Housing's strength and related demand for household goods has been a big reason why factory orders for durable goods remain firm. Although orders fell 0.8% in June, they surged 4.2% in May, and bookings for the second quarter rose twice as fast as they did in the first. That's true even though orders for capital goods slowed last quarter, suggesting that strong consumer demand took up much of the slack.

The only potential negative in the consumer outlook heading into the second half—and it's a small one—is the reversal of fortune in the stock market. Undoubtedly, earlier market gains with their attendant impact on household wealth influenced outlays, especially on big-ticket items, to at least a small degree.

But in the end, consumer spending always comes down to jobs and incomes. And unless the labor markets take a turn for the worse, there is no reason why households cannot continue to be a steadfast contributor to economic growth for the rest of the year.



JAPAN

A RATE HIKE? MAYBE NEXT YEAR

Addressing the Federal Bankers' Assns. on July 24, Bank of Japan Governor Yasuo Matsuhashita all but killed the notion that the BOJ would soon hike interest rates from their record lows, despite the economy's momentum. "For the time being," he said, "our policy will continue to be aimed at ensuring a basis for the recovery."

But while officials remain cautious, the data argue that Japan's recovery already is on firm ground. The calendar and other distortions that inflated first-quarter growth in real gross domestic product, to an annual rate of 12.7%, will cause second-quarter GDP to contract. June industrial

production fell a steep 3.9%, although July output is expected to post a sharp rebound.

Looking ahead, the mix of low interest rates, a weaker yen, and firmer job markets will support the upturns in housing, capital investment, and consumer spending, and ease the drag from the shrinking trade surplus. The June jobless rate held at a record 3.5%, but the ratio of jobs to applicants rose further, and stronger private-sector demand

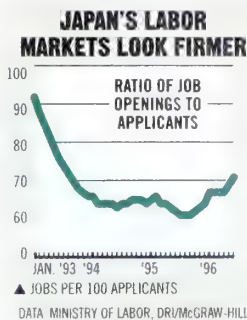
is broadening the recovery to include small businesses.

Despite growing cyclical momentum, the BOJ seems more concerned with Japan's structural problems. High joblessness is one,

because it partly reflects a mismatch of skills. Also, banks and businesses are still struggling with a mountain of bad debts. And while deflation has ended, inflation risks are scant amid so much slack in both industrial capacity and the labor markets.

Not only is the stimulus from last year's fiscal package about spent, but in 1997, fiscal policy will become outright restrictive, as the scheduled 2% hike in the value-added tax kicks in, and other measures are introduced to rein in the budget deficit, which has swollen to 6% of GDP.

Analysts expect that the BOJ will have to lift the overnight call rate on banks' borrowed funds, now about zero in real terms, by yearend, but any move on the more important discount rate is likely to be on hold until 1997.



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THE ECONOMY

SUPPLY-SIDE SOLDIER?

Dole may offer huge tax cuts, but they could hurt long-term growth

It's enough to make your head spin. In 1994 and 1995, the Republicans, and to a lesser extent the Democrats, made eliminating the federal budget deficit a central goal of economic policy. Like the ultimate economic elixir, a balanced budget was supposed to boost growth, raise living standards, and set America on the path to prosperity.

Yet the Presidential election campaign of 1996 has transformed public discussion. Now, Republican candidate and longtime deficit hawk Bob Dole seems on the verge of making a massive tax-cut plan the centerpiece of his economic program. If he does, Bill Clinton will probably start trumpeting his own, much more limited, set of tax-cut proposals.

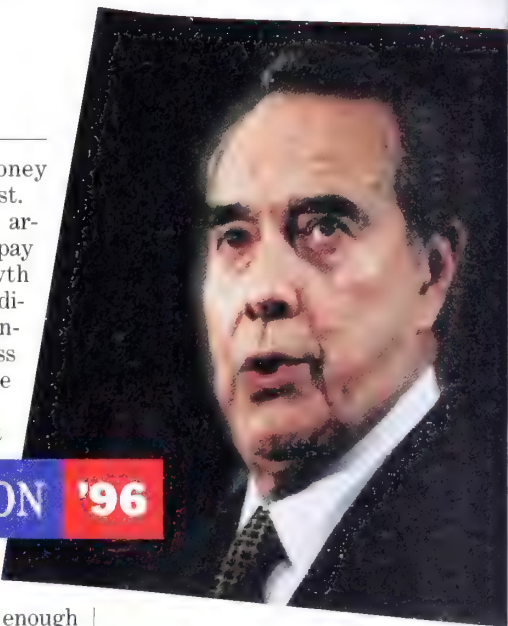
"WORSE THAN VOODOO." Will cutting taxes help the economy or hurt it? While his final plan isn't set, Dole is considering a \$600 billion tax cut over six years. The two leading options are cutting income taxes 15% across the board or rolling back the top rates imposed by the 1990 and 1993 deficit-reduction packages. The rationale: lower marginal tax rates will boost business investment and spur long-term growth. Those who get to keep more of their earnings would work more. This would boost growth without adding to inflation. Americans also would save more, since they would pay less taxes on investment income. More

savings would mean more money available for companies to invest.

Advocates of tax cuts further argue that tax cuts would largely pay for themselves. Faster growth means more tax revenue. In addition, lower tax rates would encourage households to spend less of their income on tax-deductible expenses such as housing.

Few economists dispute that these effects are real—to some extent. The problem, though, is that there is little evidence that any supply-side gains in growth would be large enough to compensate for the tax cut. Indeed, the bulk of econometric studies suggest that a tax cut such as the one being discussed could send the deficit soaring and cut business investment in the long run. Ultimately, the economy's growth rate would fall rather than rise. "You're sacrificing the long term for the short term," says David Wyss, chief financial economist for DRI/McGraw-Hill.

How do the numbers add up? Dole's economic advisers are arguing that they'll offset the \$600 billion in tax cuts with as much as \$360 billion in spending reductions and other savings. The rest, \$240 billion, or 40% of the tax cuts,

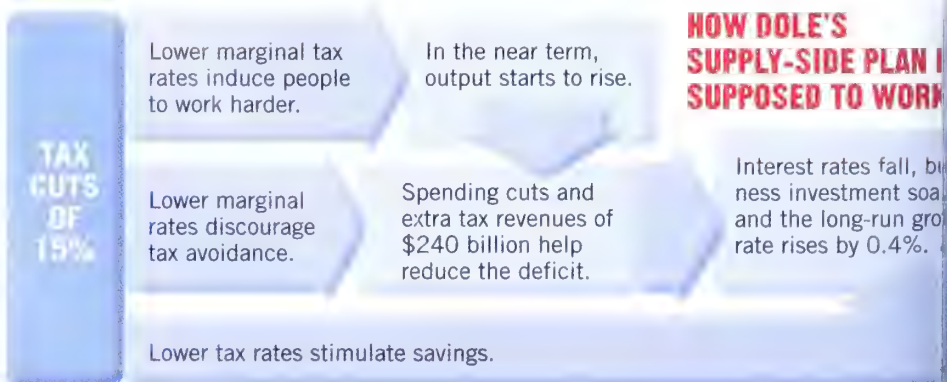


ELECTION '96

would be made up for by the supply-side "bonus."

One such potential bonus—according to a classic supply-side argument—that lower tax rates will encourage work. Many self-employed workers face a marginal tax rate of 50% or more. This can be a severe disincentive to work more hours. In a two-income family, taxes can mean that the second earner's take-home pay—even if it rises as high as \$30,000—may not cover the cost of child care.

If people put in more hours as a response to lower taxes, then the economy will grow faster without inflation. Ha



ET DOLE BE... REAGAN

Longtime GOP deficit hawk Dole seems to be morphing into a tax-cut partisan



"A \$10 billion increase in saving will not show up as any amount of measurable growth in a \$7 trillion economy," says Gale.

Rolling back the 1990 and 1993 tax increases, which mostly hit high-income taxpayers, might encourage some-

what more savings, but the change would still fail to offset the cuts.

Indeed, if the point is to spur investment, a broad-based tax cut is precisely the wrong thing to do. "What you really want to do is cut marginal rates on capital income," says R. Glenn Hubbard, an economist at Columbia University who was deputy assistant Treasury secretary in the Bush Administration. One option that Hubbard favors is a permanent investment tax credit, which "can be very potent."

ELECTION MADNESS. To be sure, the most likely immediate impact of a tax cut would be an acceleration of growth in 1997 and 1998, as Americans spent their newfound wealth. But the long-run results would be far less palatable. Overall, the more that taxes are slashed without accompanying cuts in spending, the worse the economy fares. Based on econometric estimates by DRI/McGraw-Hill, a 15% tax cut, for example, would cause the annual budget deficit to balloon to \$160 billion by 2002, 60% higher than it would have been otherwise. Interest rates on a 30-year bond would rise by 0.5 percentage points. In the long run, business investment would fall, and growth would slow, though not by a large amount. Dole campaign officials say they won't comment until their plan is final.

Of course, the situation brightens if more of the tax reductions are offset by

cutbacks in spending. DRI's analysis suggests that fully offsetting lower taxes with spending reductions could significantly boost growth over the long run. But in today's election madness, that sort of economic sanity may be too much to hope for.

By Michael J. Mandel in New York, with Mike McNamee in Washington

tax increases, which raised the top rate from 31% to 39.6%, generated little

or no additional revenue. If this is correct, it might be possible to cut this tax without losing much revenue.

But such opportunities are limited, since it's mostly high-income taxpayers who are able to shift around their income and expenses. The bottom line: A decline in tax avoidance could plausibly produce \$40 billion over six years.

That leaves some \$200 billion in tax cuts still unaccounted for. Faster growth would boost tax revenue. But based on Congressional Budget Office estimates, the annual growth rate would have to rise by 0.4 percentage points to generate this much additional revenue.

The only remaining supply-side effect that could produce such growth is the boost to savings and investment from cutting tax rates. Certainly, if investors pay less taxes on the interest and dividends they receive, they will be more willing to save.

But cutting tax rates simply does not provide a big enough bang. According to William G. Gale, senior fellow at the Brookings Institution, a 15% cut in individual and corporate tax rates would boost savings by a minuscule \$10 billion.

rd University economist Dale W. Jorgenson calculates that cuts in the marginal tax rate could have an enormous influence on people's behavior. "In that world, there are lots of things you'd do differently—you'd work more, save more, retire later," says Jorgenson. But most labor economists are far more skeptical about the gains. Most studies show that workers barely change the amount they work when their take-home pay changes. "We're talking about a very small response, far too small to make much of a difference in GDP," says Daniel Hamermesh, an economist at the University of Texas at Austin. "This is worse than voodoo economics. This is doo-doo economics." More plausible is the notion that high taxes create an incentive to find ways to avoid taxes. Studies by Martin S. Feldstein, the Harvard economist who has advised Dole, suggest that the 1993

Higher disposable income stimulates consumption.

Short-term growth rises by 0.7%, not enough to offset revenue lost from the cut.

Tax revenues fall.

The deficit begins to grow despite spending cuts.

WHAT CRITICS FEAR WILL ACTUALLY HAPPEN

DATA: DRI/McGRAW-HILL, BUSINESS WEEK

In the long run, rates rise by 0.5 points. Business investment falls slightly, long-term growth slows, and the deficit widens by \$60 billion by 2002.

STRATEGIES

THE GOP WAY IS THE AMWAY WAY

Its founders are fervent pillars of the party. Too fervent?

Is there a danger Bob Dole won't get the television exposure he needs during the Republican National Convention? Amway Corp. says yes. So the direct-sales behemoth put up \$1.3 million to help the GOP broadcast its own in-house coverage of the San Diego convention on Pat Robertson's cable-TV channel. A blatant paid-for plug for candidate Dole? "We think of it more as a public service," says Amway President Richard M. "Dick" DeVos Jr.

It's the kind of partisan public service that privately held Amway and its owners have provided Republicans for years—and one that has Democrats crying foul. At the request of the GOP, Amway gave the money to the San Diego Convention and Visitors Bureau, which bought the TV time. Democrats see that as a ploy to avoid election laws. "It is illegal for corporations to pay for what is, in essence, a Republican commercial," says David Eichenbaum, communications director for the Democratic National Committee, which plans to file a complaint with the Federal Elections Commission.

GOSPEL. It would take a lot more than opposition outrage, however, to deter Amway and its conservative founding families from playing politics. Partners Richard M. DeVos, Dick's father, and Jay Van Andel have thrown their considerable fortunes and political muscle behind GOP luminaries going back to Gerald Ford. Since 1988, figures Common Cause, the political watchdog group, Amway and its owners have poured \$3.3 million in soft money gifts into GOP coffers, including \$2.5 million in 1994 to launch the party's TV operation. Dick DeVos and his wife, Betsy, have both been courted as U.S. Senate candidates



PRESIDENT DeVOS: Amway indirectly is footing a \$1.3 million GOP bill

in Amway's home state of Michigan (the company is based in Grand Rapids), where they count Governor John Engler as a close friend and political ally. Even Amway's army of independent distributors is in on the act: Five serve in Congress and act as an informal "Amway caucus" echoing the company's gospel of free enterprise and free trade.

Amway's clout keeps growing. With the Republican Revolution in danger of faltering, the DeVoses helped out again on July 18. Richard DeVos, who was RNC finance chairman under President Reagan, was the honored guest at a GOP fundraiser in Detroit that netted \$3 million. "We're very close to the RNC," says John Gartland, Amway's director of governmental affairs in Washington. Featured speaker at the event: Bob Dole.

For all their power, Amway's founders come from humble roots. Richard DeVos and Jay Van Andel, now both retired

from Amway, started the company out of a basement in the western Michigan hamlet of Ada in 1959. The pair eventually built a worldwide organization of independent distributors of 5,000 Amway-made and branded products. An estimated 2.5 million people sell Amway goods in 76 countries. Annual global sales now top \$6.3 billion.

NO PYRAMID. Along the way, Amway has provoked considerable controversy. Under its system, distributors recruit others into the fold to sell products ranging from soap to cookware, cosmetics to smoke detectors, vitamins to encyclopedias. The "up-line" distributors collect commissions on what the recruits peddle. In 1979, the Federal Trade Commission concluded a lengthy investigation by ruling that Amway organization was not an illegal "pyramid" scheme, as critics had charged. But the scandals didn't end. In the 1980s, Amway pleaded guilty to defrauding Canada by undervaluing products it imported there. It paid \$58 million in fines and civil penalties.

Such pratfalls haven't slowed the spread of the founding families' influence in U.S. conservative circles. Jay Van Andel is a longtime trustee of the Heritage Foundation. Richard DeVos is active in the Council for National Policy, a group that includes such Reaganites as Edwin Meese. "The Amway families are conservative versions of the Rockefeller, but they do it with a fervor that makes some people nervous," says one ex-Amway staffer.

The families' zeal has not subsided as a new generation has come to the fore. Day-to-day management now handled by Dick DeVos and Van Andel's eldest son, Steve. The company policy board includes six other Van Andel and DeVos children. The political torch is carried mainly by Dick DeVos, former member of Michigan's state board of education, and Betsy DeVos, who chairs the Michigan Republican Party and serves as national Republican committeewoman from the state.

Dick DeVos chafes at the suggestion that the families—and Amway—somehow exert undue influence in GOP circles.

MEGA CLOUT

Amway, the huge direct-sales company, is throwing its political and financial weight around on behalf of Bob Dole and the Republican Party.

FRIEND OF BOB

Amway co-founder Richard DeVos was honored July 18 at a GOP fundraiser. The speaker: Bob Dole.

CONVENTION SUBSIDY

Amway gave \$1.3 million to the San Diego Convention & Visitors Bureau to fund cable coverage.

NEWT'S REVOLUTION

Amway gave \$2.5 million to the Republican National Committee before the midterm elections.

PERSONAL SERVICE

Richard DeVos' daughter-in-law, Betsy DeVos, chairs the Michigan Republican Party.

AMWAY CAUCUS

Five members of Congress are Amway distributors. The company briefs them on its stands.

we get shot at because we stand up and are counted," he says. "We have something we believe in, and we don't run for cover if we're criticized." But critics say the company amounts to an unhealthy political juggernaut. It jeers the five distributors that serve in Congress on issues important to the company. A recent article in the leftist magazine *Mother Jones* said that Represent-

tative Sue Myrick (R-N.C.), an Amway caucus member, may have received \$295,000 in campaign contributions from Amway distributors in her successful run for Congress in 1994. Myrick dismisses the article as "filled with inaccuracies" but won't comment further.

Republican leaders also are mum on Amway's TV donation. Dick DeVos calls televising the GOP gathering unfiltered

by network news organizations a patriotic gesture. Would Amway consider a similar request from Democrats to fund airtime for their convention? "They never called," he laughs. Republicans know when they ask Amway for help, the phone gets answered.

By Bill Vlasic in Detroit, with Douglas Harbrecht and Mary Beth Regan in Washington

A FUNNY THING HAPPENED ON THE WAY TO DOLE'S FORUM

The invitations were printed and mailed. For \$5,000, Republican fat cats could spend August 10 on a vintage train traveling from Oakland to San Diego with Bob Dole on the way to the GOP convention. At least 10 anted up. But then, a problem surfaced: Although the Victory Express will hit the rails on time, Dole won't be there. He never agreed to climb aboard.

As the GOP chugs its way to San Diego, party leaders are working overtime to prevent their quadrennial meeting from similarly jumping the tracks. It won't be easy. Rallies by GOP factions led by Pat Buchanan and Right to Life just outside the San Diego Convention Center threaten to upstage GOP plans for a party lovefest. And everything—from low ceilings at the convention hall to little space for vendors to sell campaign buttons—is causing strife.

DEMONSTRATIONS GALORE. Dole is trying hard to give his campaign a boost at the convention by patching up divisions in the party. Rather than repeat the Houston fracas that helped doom George Bush's candidacy, Dole is counting on a "festival of Republican ideas," says GOP Chairman Haley Barbour. The party is loading the program with mainstream Republicans, such as Colin Powell, and fresh faces, such as New York Representative Susan Molinari. There will also be a 20-minute video tribute to President Reagan. But the scripting is likely to give the convention all the spontaneity of an 11-hour infomercial. And a restless

army of reporters will no doubt look for stories elsewhere.

They won't have to go far. Buchanan, who turned down an invitation from Dole to address the convention in a 15-second videotape, will stage a rally where he will likely bash immigrant and abortion rights. Other groups plan marches to the U.S.-Mexico border and

that—more than triple its \$4.3 million contribution to the 1992 Houston confab.

As the bills have mounted, so has the controversy. Protesters persuaded a federal judge to let them demonstrate just outside the hall. Now, the Democrats plan to sue Republicans for using \$1.3 million from Amway Corp. to produce reports from the convention to be aired on the USA Network and the Family Channel. Even network executives have a beef, complaining that the Convention Center's ceiling is so low that the traditional balloon dropping will last only an instant.

To help fix the balloon problem, the GOP will build the podium a scant six feet high, instead of the tower-



SAN DIEGO: The GOP confab promises sunny skies—and plenty of strife

demonstrations in front of abortion clinics. Indeed, the demonstrations—and planned counter-rallies—have law-enforcement officials increasingly edgy: Both the FBI and San Diego police have urged local abortion clinics to close down during the convention. "San Diego has all the potential to be a Chicago, 1968"—when police brutally quelled demonstrations outside the Democratic convention—warns Sherry Bebitch Jeffe, a professor and senior associate of the Claremont Graduate School.

That may be a stretch. But just getting the hall ready and the convention paid for is already causing the Republicans massive headaches. The cost of the event is a staggering \$27 million, and the GOP has to cough up more than \$13 million of

ing stages typical of political conventions. But TV execs aren't satisfied. "The place looks like a two-thirds scale model of a real convention," says CBS News Vice-President Lane Venardos.

Dole is hoping he can close the festivities with a show of unity, gathering together on the podium all the candidates he beat in the primaries. But Buchanan, for one, has steadfastly resisted. Even if he changes his mind, "it will probably be like 1980, when Ted Kennedy wouldn't stand near Carter," says CBS's Venardos. That's a sobering thought for Republicans, who remember all too well what happened to the Democrats that fall.

By Ronald Grover in Los Angeles and Eric Schine in San Diego, with Douglas Harbrecht in Washington

CAPITOL HILL

SUDDENLY, CONGRESS IS COOKING

Both parties are scrambling to have something to show voters

Call it the Do-Something Congress. After months of gridlock, ideological posturing, and a barrage of Presidential vetoes, Republican and Democratic lawmakers are poised to wrap up their 104th session with a surprising string of legislative accomplishments.

As Congress approaches the traditional August recess, key measures that had been stalled for months are starting to move. On July 31, President Clinton pledged to sign a major overhaul of the nation's welfare system worked out by House and Senate negotiators. The welfare deal paves the way for major agreements to preserve health insurance for job-switching Americans and toughen antiterrorism measures (table).

The reason for this late rush of legislative adrenalin? "Fear," says Thomas E. Mann of the Brookings Institution. GOP lawmakers have been quaking over polls showing ebbing support for some key elements of House Speaker Newt Gingrich's Republican Revolution. Increasingly nervous about standard-bearer Bob Dole's prospects, GOP incumbents "know they have to come home with something to show for their work," contends Mann. Adds Norman J. Ornstein of the American Enterprise Institute: "Congress is like a marathon. You pick up the pace because you know you're going to be judged on your ending."

INTERCEPTION. Of course, Republicans aren't the only ones trying to burnish their records. Clinton cut the last-minute welfare deal partly because he was worried he'd be roasted for not honoring his promise to "end welfare as we know it." The move clearly has unsettled the Dole camp. "There's no doubt that a welfare-reform bill takes a huge chunk of Dole's message," grouses one GOP strategist.

Liberals aren't thrilled by Clinton's decision to sign a bill that would end the poor's open-ended entitlement to

welfare. But many see a silver lining in the Republicans' move toward their position on other measures, such as health-care portability, environmental cleanup, and hiking the minimum wage. "Remember, they are passing Democratic initiatives," crows Senate Minority Leader Thomas A. Daschle (D-S.D.).

Republican leaders, naturally, claim the Democrats have made the bulk of

ings Accounts—IRA-like funds that can be used to buy insurance—and Republicans agreed that the accounts be tested first in a pilot project. That accord had a domino effect, encouraging House and Senate conferees to move forward on Clinton's call for boosting the minimum wage from \$4.25 per hour to \$5.15 an hour and giving small business some modest tax cuts.

OUTMANEUVERED. It's quite a change from the in-your-face style of legislative combat favored by Gingrich & Co. But the 104th Congress has been one prolonged nosebleed for outmaneuvered Republicans. The GOP managed to make some symbolic reforms in congressional procedures and passed a landmark farm reform bill that phases out traditional subsidies over seven years. Republican

LET'S MAKE A DEAL

The outlook for key measures on Capitol Hill



HEALTH INSURANCE Congress has cleared the way for health-insurance reform that would allow workers to keep their insurance when they move from job to job.

MINIMUM WAGE A bill that would increase the minimum wage from \$4.25 an hour to \$5.15 an hour by July 1, 1997, is expected eventually to be signed into law.

TAX CUTS Congress will probably approve a tax cut for business of at least \$7 billion over the next eight years. It will restore tax credits for research and development and assistance for employer-provided education.

TERRORISM Antiterrorism legislation that would expand police powers to monitor telephone calls of suspected terrorists is likely to pass both houses of Congress and probably will win support from the White House.

WELFARE On July 31, President Clinton pledged to sign an overhaul of the nation's welfare system that shifts responsibility to the states. The bill is quite tough: It even cuts benefits for legal immigrants.

the concessions. But GOP leaders also are finding it increasingly difficult to hold nervous rank-and-file lawmakers in line. Plus, Dole's departure from his post as Senate Majority Leader and the ascension of his dealmaking successor Trent Lott (R-Miss.) have made compromise easier. Lott figures Congress' late burst of activity will be a boon to all Republicans come November. "If we can get these done, we'll deserve an Olympic gold medal," he says.

One of the biggest breakthroughs came over plans to guarantee health-care portability. On July 25, Senator Edward M. Kennedy (D-Mass.) and Representative Bill Archer (R-Tex.) cut a deal in which Democrats accepted GOP demands for some role for Medical Sav-

also got a sweeping telecommunication deregulation bill passed. But the GOP has big goals, including term limits, a balanced-budget amendment, tax cuts for families and investors, legal reform, and major regulatory overhaul, bit the dust.

With the new mood of conciliation congressional Republicans hope to shed the "extremist" label pinned on them by Clinton. Democrats, among the pollster Robert Schroth, assert that the transformation is "too little, too late." But, heartened by recent polls that show the Democrats' lead narrowing, November approaches, many GOP loyalists hope their shift has come just in time to preserve the Republican majority—and their hides.

By Mary Beth Regan in Washington

By Lee Walczak

CAMPAIGN-FINANCE REFORM NEEDS A MIRACLE

At first glance, a lawsuit alleging that the Christian Coalition is engaging in unlawful political activity looks like another thunderbolt from the heavens aimed at Bob Dole's struggling Presidential campaign. The 1.7 million-member coalition, a wing of televangelist Pat Robertson's empire, has been a mainstay of Dole's election bid. But on July 30, the Federal Election Commission filed suit against the group, charging that its distribution of millions of highly partisan "voter guides" amounted to illegal contributions on behalf of Republican candidates.

Though a coalition spokesman denounces the charges as "baseless," the suit could hobble the organization's plans to mobilize behind Dole and GOP congressional candidates this fall. Its efforts are particularly critical in the South and West, where Dole's lead over Bill Clinton isn't as solid as it should be.

REVERBERATIONS. Longer term, new government scrutiny of politicking by right-wing advocacy institutes and research foundations could reverberate beyond the FEC. The Internal Revenue Service is looking at whether the coalition's unabashedly pro-Republican organizing is cause for denying the group its favored tax-exempt status.

Before liberals rejoice at the coalition's presumed day of reckoning, they would be wise to study their history. The FEC has a dreadful record at winning suits over "voter education" issues. During the past 20 years, "the FEC has systematically lost in court" on similar cases, says Jan W. Baran, a GOP election-law expert with Wiley, Rein & Fielding in Washington. This year alone, the FEC lost cases against GOPAC, Newt Gingrich's political arm, a Maine right-to-life group, and, in a June Supreme Court ruling, the Colorado Republican Party.

In the past seven years, it has lost lawsuits involving the National

Organization for Women, the Christian Action Network, and war foe Dr. Benjamin Spock. The trouble, Baran contends, is that the FEC's claim that any advocacy group's consultation with a campaign is illegal is just too broad. "If that's a legal standard, a whole lot of people are in trouble," he asserts, mentioning such liberal organizations as the

the deal—presumably because he had been promised entrée into a future Dole White House.

The upshot: The Christian Coalition has done about all it can do for Dole's blighted Presidential drive. Dole considers his conservative base sewn up and is making a mad dash to the center to woo straying moderates and suburban independents.

All that remains for Reed's righteous armies to do is to turn out on Election Day and pull the lever for Dole, something coalition members are already disposed to do.

TRAVESTY. The big lesson from the FEC's attack on the coalition is not the chilling effect that it will have on Bob Dole's Presidential bid. Instead, the coalition's thinly disguised partisanship only underscores the travesty of campaign-finance laws.

This year, all pretense of compliance has vanished, as the Clinton and Dole campaigns openly ignore the rules and grow ever bolder in their quest for special-interest money. In his book, *The Choice*, Bob Woodward alleges that Clinton personally steered

Democratic Party money toward states where it would do his political cause the most good. And since Dole is currently broke, his preconvention travels are being funded by the Republican National Committee under the flimsy pretense that Dole is raising money for committee causes.

The likely prospect that the Christian Coalition, joining a host of groups of all political stripes, will be able to dance away from FEC sanctions and continue its questionable behavior only makes the problem of eroding compliance with election laws more acute. And it makes it even more imperative that the issue the politicians wish would go away—campaign-finance reform—gets elevated to the top of the national agenda in 1997.

Walczak is *BUSINESS WEEK's* Washington bureau chief.



Ralph Reed & Co. may dance away from FEC sanctions, making campaign-finance reform imperative

Sierra Club, the AFL-CIO, and gun-control advocates.

Meanwhile, the Christian Coalition has already done most of its heavy lifting for the Dole campaign. For starters, Coalition Executive Director Ralph Reed embraced Dole early in the nominating season and lobbied hard to keep restive members from backing conservative firebrand Pat Buchanan. After some early defections, the flock came home, and votes of coalition members helped seal Dole's breakthrough defeat of Buchanan in the South Carolina primary.

Next, Reed and Dole brokered an agreement that gave the Kansan the leeway to try and finesse the abortion issue by tacking a "tolerance clause" onto the staunchly pro-life Republican platform. Other anti-abortion groups called Dole's maneuver reprehensible, but Reed blessed

EXECUTIVE SUITE

THE ANGRY ANGELS AT ZENITH

The Koreans rescued Zenith. Now they want results

Last November, spirits were running high as more than 100 members of Zenith Electronics Corp.'s senior management group gathered in the company cafeteria in Glenview, Ill. LG Electronics Inc., the Korean consumer electronics giant once known as Lucky Goldstar, had just invested \$351 million in the company in exchange for a 58% equity stake. Hun Jo Lee praised Zenith's management and singled out Albin F. Moschner, Zenith's CEO and president, for kudos. "It was pretty clear to me they thought very highly of Al," says Gerald M. McCarthy, Zenith's former executive vice-president for sales and marketing, who attended the meeting.

How things change. On July 24, Moschner, 43, abruptly resigned from Zenith. Officially, the choice was his. He stepped down to pursue "personal business interests," according to a statement the company attributed to him. Hyo Chul Chang, a general manager of LG and a member of ZEST—Zenith Electronics Support Team, says Moschner's departure was unexpected. But many people inside and outside the company doubt Moschner's decision to go was entirely his own. "Baloney," says Robert G. Gutenstein, an analyst with Kalb Voorhis & Co. Moschner did not return calls seeking comment.

RED INK. Most telling, Zenith acknowledges that Moschner will receive a \$4.3 million payment required in the company proxy for Moschner if he is terminated. Peter S. Willmott, a Zenith director who is acting as interim CEO and president, says Moschner deserves the money because of his service to the company. But he stops short of saying that Zenith was not obligated to pay it. "You would need a lawyer to figure that out," he says.

If Moschner had a falling out with LG, it's an ironic twist. The former CEO is credited with bringing in the Korean concern to help save what was then the last American-owned television maker. Zenith has lost money on op-

erations every year since 1984. But in Zenith, LG saw a valuable brand name and a company with strong U.S. market share.

Still, sources say the Koreans were shocked by the losses Zenith continued to rack up, caused in part by high operating costs. For 1995, Zenith lost \$92.4 million on sales of \$1.27 billion—about double, sources say, what the Koreans had anticipated. "The loss was larger than they initially expected," says Kell B. Benson, Zenith's former chief financial officer, who left the company last November. "I assumed they were unhappy with it." Red ink continued to spill this year, with Zenith losing \$68.5 million through June.

NET CRUISERS. Control may also have been an issue between Moschner and his bosses. At first, Korean executives said they wanted Moschner and his team to run the company. But this spring, Kisong Cho, LG Electronics' managing director of corporate planning and strategy, began spending two weeks a month at Zenith headquarters. "He looks at our financing, [and] he makes sure that we use whatever synergies we can" to keep costs down, says Willmott. Another LG veteran, Michael Ahn, has taken over as senior vice-president of operations.

Moschner's paycheck was another source of tension. He received a base salary of \$423,333 and other compensa-

tion of \$370,400 in 1995, according to Zenith's proxy, which compensation experts say is in line with pay packages for chief executives at similar companies. Sources close to the board say the aggressive and outspoken Moschner thought that he deserved a raise in 1996. But as part of the LG acquisition, Zenith had already hired He-



LOSS LEADER

Moschner wanted a raise despite Zenith's poor performance; instead, he will get a \$4.3 million severance payment

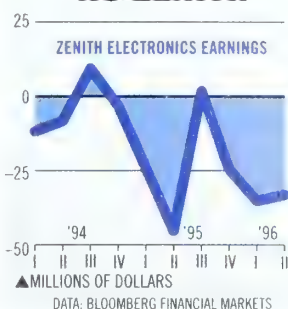
witt Associates to recommend a new compensation plan for top executives.

Moschner's departure adds to the turmoil at a company in desperate need of turnaround. Its core TV business continues to lose money despite years of cost-cutting, and despite employment dropping to 16,200 from 24,900 at the end of 1992. The company's stock tripled three months ago on news that Zenith was working on Internet-related products such as cable modems and television that can cruise the Net. But few expect significant revenues from those ventures anytime soon. "It's one thing to announce. It's another thing to start selling products," says David Bach, investment officer for California Public Employees' Retirement System, a major Zenith investor.

Key to Zenith's future will be the yet unidentified CEO who permanently replaces Moschner. Willmott, who is leading the search, says Zenith has strong prospects in new ventures. As he says the financing, distribution, and technical expertise of LG Electronics will help. "I'm very bullish about this relationship," he says. Now, he just needs to find an executive who agrees with him.

By Peter Elstrom in Chicago

NO ZENITH



AND THEY SAY AUDIENCES ARE FICKLE

How-biz stocks keep getting hammered, even on good news

Once upon a time, Wall Street loved the entertainment biz. But these days, anything the media/entertainment companies do—even announce good news—generally elicits groans. Take Walt Disney Co. On July 25, the company said that second-quarter earnings were up 26%, including results from its recently acquired, troubled ABC television network. Its stock fell 3%, to 52 1/2 that week. Shares have since edged a bit, but they remain near their 52-week low. Then there's Time Warner.

On July 16, the Federal Trade Commission finally agreed in principle to the merger with Turner Broadcasting System Inc. Time Warner's stock jumped 12%, to 37 1/2, in the days following the agreement—then quickly slipped to near its 52-week low.

All that followed a pattern set by Viacom, which in June announced that the Inter-Continental Revenue Service had finally approved the \$1.7 billion sale of its cable channel. Its stock hiccuped, then headed south. It was helped by Viacom's July announcement that its third-quarter earnings from licensing operations fell 41%, but \$23.3 million on revenues that rose 3.1%, to \$2.85 billion. The stock is now trading 4 1/2% also near recent lows.

Some seasoned media-stock chasers are grumbling that this may be the start of a prolonged downturn. The "euphoria" over the multiples paid for media properties "is fading," says Schroder Wertheim Co. media analyst David Londoner, though he predicts that "two years from now, [media stocks] will be darlings again." Investor Mario J. Gabelli, whose Gabelli Global Interactive Couch Potato Fund of entertainment stocks is down nearly 10% since early June, says the

market has turned so quickly and unpredictably against some entertainment stocks that he has felt at times as if he has been "shot between the eyes."

An intractable downturn would be dispiriting indeed. The media megadeals of the past two years were supposed to reenergize the industry. Time Warner offered \$7.5 billion

of putting these big assets together."

The flaw in many bulked-up companies' strategies, says Bankers Trust Securities Corp. analyst Mark McFadden, was a belief that programs and movies would quickly become much more lucrative as distribution channels, such as direct-satellite broadcasting, emerged. "People thought it was all about producing content. It's not. It's about producing desirable content," says McFadden. As entertainment companies race to spend more to improve their offerings, "people in the delivery business have been able to cherry-pick the best stuff," he says.

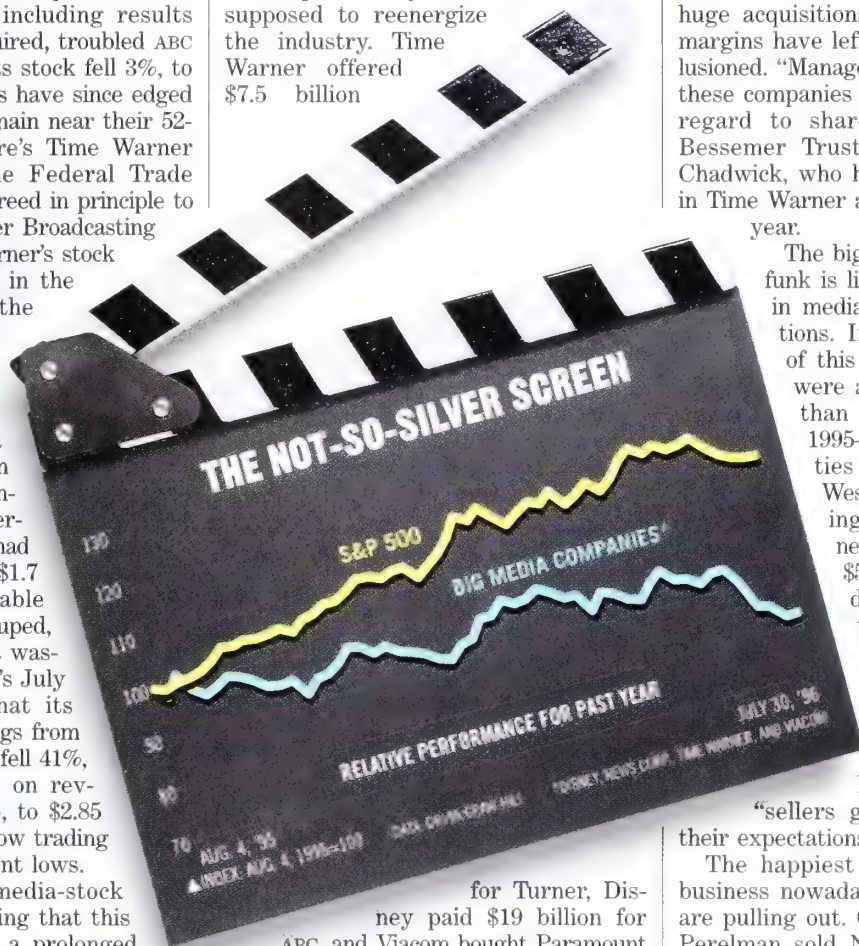
"FIEFDOMS." Big entertainment companies' inability to quickly absorb their huge acquisitions and generate fatter margins have left many investors disillusioned. "Management continues to run these companies as fiefdoms, with little regard to shareholder value," says Bessemer Trust Co. executive John Chadwick, who has held sizable stakes in Time Warner and Viacom in the past year.

The big fallout from the stock funk is likely to be a slowdown in media mergers and acquisitions. In the first six months of this year, 366 media deals were announced—10% fewer than in the last half of 1995—according to Securities Data Co. Now, US West Media Group's pending acquisition of Continental Cablevision Inc. for \$5.3 billion in stock is under pressure because of the 23% drop-off in the bidder's share price.

Even when stocks plunge, says Steven Rattner of investment bankers Lazard Frères & Co., "sellers generally don't adjust their expectations downward."

The happiest people in the media business nowadays may be those who are pulling out. On July 17, Ronald O. Perelman sold New World Communications Group Inc., a bush-league TV-show producer and owner of 10 Fox-affiliated TV stations, to Rupert Murdoch's News Corp. for \$2.5 billion. New World had been trading at 15%; Murdoch paid \$27 a share. Wall Street's reaction? After the deal was announced, News Corp.'s shares fell 7%. Groan.

By Elizabeth Lesly in New York



for Turner; Disney paid \$19 billion for ABC, and Viacom bought Paramount Communications Inc. for \$9.9 billion. Last summer, Seagram Co. sold its huge stake in DuPont Co. for \$7.7 billion aftertax and bought 80% of MCA Inc. for \$5.7 billion. Despite a deal announced on July 30 to sell German rights to MCA's TV shows and movies for \$2.5 billion, Seagram's shares are off 10% in the past year. Sighs one senior entertainment executive: "Investors are questioning the very premise

"People thought it was all about producing content. It's not. It's about producing desirable content"



MOUSSOURIS: He still plans on licensing his chip technology

SILICON VALLEY

IS THIS END RUN GOING NOWHERE?

MicroUnity's challenge of Intel looks mighty shaky

Ever since chip-industry insiders got wind of what John Moussouris was up to, they have said he was crazy. Little wonder: The founder of MicroUnity Systems Engineering Inc. wanted to make an end run around mighty Intel Corp. with a new chip that promised 100 times the speed of Intel's Pentium at just one-tenth the price. With some \$130 million in backing from Microsoft, Tele-Communications, Time Warner, Motorola, and other giants, Moussouris predicted his "mediaprocessors" might spawn a generation of multimedia gear to rival PCs.

These days, 8-year-old MicroUnity is looking shaky. Burning through almost \$4 million a month and unable to raise additional money, it has been forced to close down its \$60 million manufacturing plant and lay off all but a skeleton staff. That's quite a reversal for the charismatic Moussouris, 46. A Rhodes scholar and former roommate of William Randolph Hearst III at Harvard University, he co-founded MIPS Technologies Inc., a company that developed the microprocessors that are currently used by Silicon Graphics, Nintendo, Sony, and others. Now, he concedes, "nothing is certain."

INJECTING SMARTS. Ambition may have gotten the best of Moussouris. MicroUnity's plan relied on a risky new chip-making process, and he insisted on building an expensive factory, which is an unheard-of undertaking for a startup. Moussouris' technology road map was also flawed. His chips were supposed

to inject more smarts into everything from television settop boxes and cable modems to digital cellular telephones—thus blunting the charge of Intel-based PCs into multimedia and communications. But these potential target markets failed to develop. In addition, the chips proved difficult to manufacture. Last spring, Moussouris sought more equity financing, bringing in investment

bankers to assess options, such as going public. Instead, they advised him to scale back.

Moussouris insists that his dream is still alive. He plans to license MicroUnity's technology to makers of cable modems, cell phones, and other devices. But that may not be easy. Observes Alexandre Balkanski, CEO of multimedia chipmaker C-Cube Microsystems Inc.: "I don't think he understands the nitty-gritty, day-to-day pressures of running a successful company." Maybe, but he's going to have to learn fast.

By Robert D. Hof, with Andy Reinhardt, in San Mateo, Calif.

ADVERTISING

THE OLD MAN AND THE 240Z

Nissan reaches into its past to raise its profile in America



For Yutaka Katayama, the recognition has been a long time coming. Katayama, known as "Mr. K" to his colleagues and friends, founded Nissan Motor Corp. USA, the Japanese company's American subsidiary in 1960, and built it into a behemoth that sold nearly a half-million vehicles a year by the time he retired in 1977. On Aug. 4,

during the broadcast of the closing ceremonies of the Olympics in Atlanta, Nissan will launch a massive \$200 million television advertising campaign aimed at establishing its name, on and for all, as a prominent U.S. brand. It also will introduce a new character to represent the company in the campaign: a grandfatherly Japanese man who embodies the optimism of the original Mr. K.

If you've been watching the Olympics, you've probably met him already. He's the one in the Datsun baseball cap, who, in a series of teaser ads, delivers such simple messages: "Smile" and "Drive Happy." Once the full-scale campaign starts, Dale Ishimoto, the 73-year-old Japanese-American actor who plays Mr. K, will cameo in a series of fanciful ads.

Full of hip, tongue-in-cheek humor, the campaign also aims to recapture the Datsun heritage. Nissan phased out Datsun in the early 1980s because it wanted to be known by a single name worldwide. Insiders now think botched the shift. "We essentially walked away from all that existed under Datsun," admits Nissan President Robert J. Thomas. "Getting our past back will add to our credibility, our personality."

ONE OF THE COOLEST CARS. TWBA Clark/Day Inc., Nissan's ad agency, hopes to turn Nissan's likeable old man into an icon. The new campaign deliberately combines fiction and fact. The character only vaguely reflects the real Mr. K, mainly to harken back to the days when the Datsun 240Z sports car was one of America's coolest cars. But Nissan also may distribute information on the real Mr. K through its dealer

Katayama, now 87 and living in Tokyo, is a bit of a character himself. He makes and flies kites as a hobby, and he loves America (when he left the U.S., his Christmas card mailing list contained 20,000 names). "I was there 40 years, so Japan was kind of a blank for me," Mr. K says. He is bemused by the

DATSUN DAYS: Evoking the spirit of Nissan USA ex-chief Mr. K

new ads. "It was disappointing when I was pulled back to Japan," he says. "But I'm very happy that someone recognized what I did 20 years ago. Someone? Make that hundreds of millions of TV viewers, if Nissan's new ads do the job."

By Larry Armstrong in Los Angeles, with Edith Updike in Tokyo

medal or not, few athletes will leave empty-handed.



A black and white photograph showcasing a variety of packaged products. On the left, a pair of cowboy boots sits atop a stack of clothing, including a t-shirt with 'Atlanta 1996' printed on it. Below the boots is a box of 'HOT B-B-Q SAUCE'. In the center, a large bag is labeled 'GAMES'. To the right, a box of 'Georgia Peaches' is visible, along with a jar of 'Peaches' and a small stuffed animal. The background is a plain, light-colored surface.



We answer to the world

PEOPLE

HOST WITH A PAST

President Clinton's vacation plans may raise eyebrows

Certainly, Jackson Hole, Wyo., is a stunning spot. Even so, President Clinton's decision to vacation from Aug. 9 through Aug. 17 at Max C. Chapman Jr.'s Bar-B-Bar ranch has left some Wall Streeters scratching their heads: Clinton will be spending his time with an ardent Republican who has drawn the critical attention of securities regulators.

From 1989 to May, 1996, Chapman was the chief executive of Nomura Securities International, the U.S. unit of the giant Japanese broker. He is now nonexecutive chairman. Nomura and Chapman were investigated from 1992 to 1995 by the New York Stock Exchange for a possible failure-to-supervise charge. At issue was whether Nomura permitted some \$212 million of trades in violation of the exchange's net capital rules. On Nov. 29, 1995, the firm, while neither admitting nor denying guilt, paid a \$1 million fine, the third-largest in NYSE history.

When Chapman was CEO of Nomura, he had an unusual arrangement whereby



CHAPMAN: While CEO of Nomura, he ran two independent ventures for his own benefit

he established and ran two unpublicized ventures for his own benefit, independent of Nomura. Chapman's primary operation was the Moran Group, an investment firm he formed in October, 1992. The main investor in Moran was Wolfgang Flöttl, a secretive Bahamas-based investor married to a granddaughter of President Eisenhower. Moran raised eyebrows within Nomura because Chapman used to execute trades for Moran while he was CEO of Nomura, which left him open to conflict-of-interest charges. It wasn't until October, 1993, that Chapman's Japanese bosses got him to agree to formal oversight of his personal trading. Chapman declined comment, but a spokesman says all Moran trades were disclosed to Nomura.

Nor was Chapman always a Clinton fan. As a conservative Republican, he has been known to criticize the President and his liberal policies at Nomura's Monday morning meetings for about 30 senior executives, say some of those who attended the meetings.

MUTUAL FRIEND. Such talk stopped, however, after Chapman met Clinton last summer, when the President was vacationing at the ranch of Senator John D. Rockefeller IV (D-W. Va.), which is next door to Chapman's. Erskine Bowles, formerly Clinton's deputy chief of staff and a mutual friend of Chapman and Clinton, introduced the

two. Chapman, an excellent golfer, played golf with the President, and hosted the Clinton family for lunch at his ranch—a 1,200-acre stretch bordered by the Snake River at the foot of the Grand Teton Mountains. And since then, he has attended a state dinner and slept over at the White House.

As a guest of Chapman, Clinton will not pay rent, says White House spokeswoman Mary Ellen Glynn. And there is "not a need to report personal hospitality on one's income tax," she says. Chapman will not be at the ranch when the Clintons are there, says Glynn. But Chapman will be nearby and he plans to play golf with the President in the mornings.

By Leah Nathans Spiro in New York

PEOPLE

THE FIRST—AND LAST—GOLD?

Hong Kong stops to savor Lee Lai-Shan's Olympic victory

It's Hong Kong's first Olympic medal—and it may be its last. Twenty-five-year-old windsurfer Lee Lai-Shan's historic gold-medal victory in the Atlanta games marked the only time a Hong Kong athlete has stood on the victor's stand since the British colony first sent athletes to the Olympics in 1952. And with China set to resume sovereignty over the city of 6 million on July 1, 1997, it's an open question whether Hong Kong will ever field its own team again.

Lee's victory filled the front pages of major Hong Kong papers, supplanting stories about the bickering and unease surrounding Britain's imminent depart-

ure from the colony. Even a Chinese test of nuclear weapons took second billing, as newspapers celebrated the victory by San San, as the Olympic champion is known at home. Normally phlegmatic commuters lingered around television screens in subway stations, watching as *God Save the Queen* was played during the July 29 medal ceremony.

Lee, the eighth of 10 children, whose family still lives on Cheung Chau, an isolated outlying island of 22,000 people, has been showered with awards. Prominent businessman Henry Fok gave her

WIN-SURFER

Booty from admirers includes free travel, \$300,000, and a lifetime supply of rice

a gold bar worth \$13,000. And a sortment of local businesses have promised San San at least \$300,000. Cheung Chau officials may even construct a statue of her on the island. A food importer promises a lifetime supply of rice.

As for transportation, Lee won't have to windsurf to get around. Cathay Pacific Airways Ltd. has given San San five years of unlimited free flying. The operators of the ferry service that runs to Cheung Chau say that the champion will never have to pay to ride again. And Hong Kong's sparkling subway system will also be free for life for San San—as long as she leaves her sailboard at home.

By Mark Clifford in Hong Kong





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In Business This Week

EDITED BY KELLEY HOLLAND

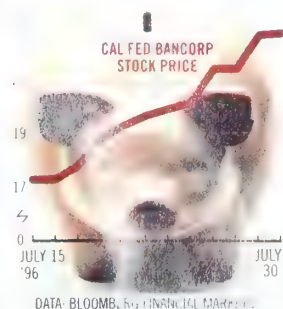
SPLITSVILLE TALK IN THE AIR

USAIR AND BRITISH AIRWAYS may be headed for divorce court. In a suit filed July 30 against BA and its prospective partner American Airlines, USAir accused BA of violating its 1993 alliance with ailing USAir, in which BA holds a 24.6% stake. USAir claims that BA's plans to create an alliance with American violate U.S. antitrust laws and breach BA's fiduciary duty to USAir. It wants BA, which invested \$400 million in USAir, to give up its board seats. Lehman Brothers analyst Brian Harris says USAir may be trying to improve its own marketing deal with BA. And if the partners do split, USAir's new management would

CLOSING BELL

BANK BEAU

Wedding bells finally are starting to ring for California's midsize banks. On July 29, Ronald Perelman's First Nationwide Holdings agreed to pay \$1.2 billion for Cal Fed Bancorp of Los Angeles. Investors rejoiced as Cal Fed's stock rose 6% to close July 30 at 22 $\frac{1}{2}$, within sneezing distance of Perelman's 23 $\frac{1}{2}$ per share offer. Bargain hunters beware: Analysts say many midsize California bank and thrift stocks are now "pricy."



"have all the flexibility to do what they want," he says. American and BA say their proposed deal would not violate the BA-USAir pact.

MINORITY LENDING IS ON THE RISE

FOR YEARS, "COMMUNITY Reinvestment Act" were three of the most hated words in banking. But lenders finally have figured out that there's money to be made in America's inner cities. Mortgage loans to blacks rose by 9.7% in 1995, to 138,034, according to Home Mortgage Disclosure Act data released on July 30. And lending to Hispanics grew by 4.1%, even as overall mortgage lending dropped 8%. True, denials of minority loans also shot up: 40.5% of blacks were turned down, up from 33% in 1994. But even housing advocates say that largely reflects a pickup in applications.

KIDDIE RADIO TAKES A HIT

KIDDIE PROGRAMMING IS THE talk of television, now that the networks will be providing three hours of educational shows a week. But at Children's Broadcasting, it's a different story. Between July 29 and July 31, investors sent the radio company's stock down from 7 $\frac{1}{2}$ to 6 after the ABC Radio Network ended an agreement to provide sales and marketing support to Children's. One possible reason for the termination: ABC and its parent company, Disney, may be gearing up to launch their own children's radio-programming operation.

AETNA'S ADIEU TO MEDICARE

AETNA IS BAILING OUT OF a big part of the Medicare business. The company has

HEADLINER: ROBERT PALMER

'BLOODY KNEES' AT DEC

Robert Palmer is on the spot—again. Digital Equipment ended fiscal 1996 with a net loss of \$112 million on sales of \$14.6 billion. Despite four years and \$1.2 billion in restructuring charges to cut its staff in half, DEC still lags rivals in profitability per employee.

Palmer, 55, a long-distance runner who became CEO in 1992, tries a sports analogy to explain the latest setback. "We're going to stumble sometimes and bloody our knees," he says. "The point is to get up and get on with it." But aside from taking a \$492 million

restructuring charge and shedding another 7,000 workers, Palmer's plan is short on specifics.

In the next few weeks, analysts expect DEC to announce a partner to help make its desktop PCs, a move Palmer doesn't rule out. Meanwhile, DEC's board on



July 30 authorized a buyback of up to 10 million shares. But the alliance won't carry DEC around the track. And the buyback covers roughly only as much stock as Fidelity Investments dumped this spring en route to halving its DEC holdings.

By Paul Judge

decided to leave the business of processing fee-for-service Medicare claims to the federal government. The reason: After purchasing U.S. Healthcare, Aetna decided to concentrate solely on managed health care instead of the government-funded variety, which can be big business but comes with slim profit margins. About 1,700 Aetna claims processors will lose their jobs. But the company says that some of the employees should be hired by the company or agency that takes over the government work.

PALMY DAYS FOR GE IN BERMUDA

SCORE ONE FOR GENERAL Electric. A judge in Bermuda has ruled that the liquidation of Electric Mutual Liability Insurance, a mutual insurer owned by GE, can go forward. Last October, just four

months after EMLICO moved from Massachusetts to Bermuda, the company filed for liquidation after identifying a massive potential environmental liability. Reinsured to reverse EMLICO transfer to insurer-friendly Bermuda, contending it was done to give GE an advantage in collecting reinsurance bills after liquidating. For now they look to be out of luck. But they are still pursuing lawsuits that would reverse the Bermuda move.

ET CETERA...

- IBM will add \$380 million to a \$500 million investment in its disk-drive business.
- Monsanto is raising its Cargill stake to a controlling 54.6% and replacing the CEO.
- The Interior Dept. may trade land for a Crown Butte gold mine near Yellowstone.
- Absolut vodka is back on retailers' shelves in Sweden after a poisoning scare.

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EDITED BY DOUGLAS HARBRECHT

TELECOM: THE FEDS HAVE ANOTHER TOUGH CALL TO MAKE

The Baby Bells howled in early August when the Federal Communications Commission set down strict rules specifying exactly how the regional phone companies must open their local monopolies to long-distance rivals. But the wailing has just begun. A bigger fight is brewing over an even thornier issue in the Telecommunications Act of 1996: overhauling the subsidies that keep consumer phone rates low.

At issue is the \$30 billion in so-called access charges that local carriers collect from long-distance companies such as AT&T and MCI Communications. Those charges, ostensibly for connecting to the local customer, are artificially high—for a reason. They help local carriers subsidize cheap residential phone service. But under the 1996 law, access charges are slated for deep cuts. And the FCC has only until May, 1997, to devise a new system for keeping local rates affordable for everyday phone users. "The fight over local competition rules was a gentleman's spat compared to the food fight we'll see over this," says Scott Cleland, managing director at the Washington Research Group.

POOLING FUNDS. Even the Bells concede access charges must come down. While they average about 6¢ a minute, rates will have to drop closer to the actual cost of the connection service, which the Bells say is 1.5¢ and AT&T contends is less than a penny. Congress, loath to make the tough call on how to replace the current subsidy system, punted to the FCC the task of creating a new formula. "It's just an impossibly complex job," sighs FCC Chairman Reed Hundt.

The most critical decisions: What level of basic service should be made affordable for all Americans and at what cost? One approach is to have the entire industry contribute to a "universal service" fund used to lower residential rates.

The Bells, which at least initially would benefit most from

industry-funded subsidies, contend it takes \$20 billion annually to keep local rates at their current low levels. That helps knock the average household phone bill down about \$11 per month, the Bells figure. But AT&T and MCI say the Bells are lining their pockets, and the real cost is closer to \$6 billion.

Moving to entice the FCC, MCI and AT&T have vowed to pay on any reduction in access fees directly to their phone customers. But Robert T. Blau, vice-president of regulatory affairs at BellSouth Corp., argues: "Very little of that will filter through to consumers." In fact, the Bells warn a misstep in this process could force local rates up. Gerry Salemme, vice-president of government affairs for AT&T, scoffs at such predictions as "specious claims."

The sniping has made members of Congress edgy. After all, many of them heralded the telecom bill as opening the door to interstate competition that would lower rates. So lawmakers will be leaning hard on the FCC to ensure that consumers in rural and low-income communities don't get slammed with hikes. "If local rates are going up, we will probably take corrective action," vows Representative Rick Boucher (D-Va.).

For now, the Bells have staved off an imminent hit. The FCC isn't expected to allow long-distance companies to dodge access fees until after next year's rulemaking at the earliest. Still, there's no question the fees eventually will fall sharply. And under any revamped system, local carriers will be picking up more of the tab to subsidize residential service—eroding their pricing advantage against new competitors for local service. Add that new FCC rules forcing local carriers to give long-distance and wireless phone competitors cheaper access to their systems, and competition may soon be burning up the wires.

By Amy Barrett



HUNDT: A "complex job"

CAPITAL WRAPUP

SECRETARY COLIN POWELL?

► With retired Joint Chiefs of Staff Chairman Colin L. Powell refusing the GOP Vice-Presidential nomination, former President Gerald R. Ford has come up with another way to get the ex-general on Bob Dole's team in time for the Aug. 12 kickoff of the Republican National Convention. Ford is urging Dole to couple his announcement of who will be his running mate with an added surprise: naming Powell as his choice for Secretary of State in a Dole Administration.

TIME SLIPS FOR FDA REFORM

► Efforts to revamp the Food & Drug Administration may have to wait until next year. Representative James C. Greenwood (R-Pa.), head of the GOP's task force on FDA reform, has postponed action until after the August congressional recess. FDA officials are resisting a bill aimed at speeding product approvals. They fear it will weaken public safety by requiring outside product reviewers and by allowing companies to promote products for unapproved uses.

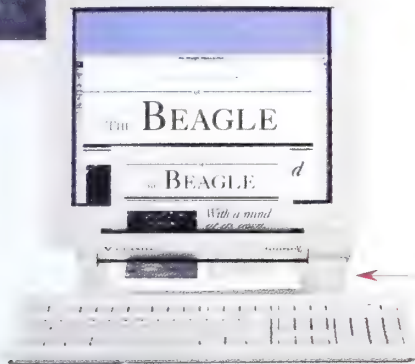
ELEPHANT STOMP

► Top Republicans are nervously awaiting the mid-August release of political consultant Ed Rollins' memoirs—just in time for the opening of the party's San Diego convention. Why? The ex-political adviser to Ronald Reagan and Ross Perot takes swipes at virtually all the GOP's heavyweights, from Bob Dole and Newt Gingrich to George Bush and Nancy Reagan. Fumes one senior Republican: "The guy must have a death wish."

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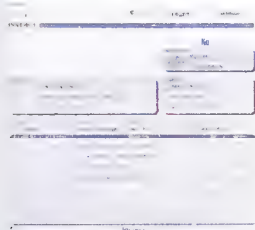
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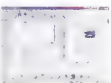
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INDONESIA

TREMORS IN JAKARTA

Will political uncertainty stall Indonesia's economy?

The worst riots in Jakarta in two decades have shaken attorney Mulya Lubis. At the entrance of his office in the swank steel-and-glass Wisma Bank Dharmala office tower, soldiers bearing automatic weapons are now posted. Lubis, who does pro bono work for human rights groups, worries the already tense situation could get worse. "When things run amok, nobody will be able to control them," he frets. "I wonder how long the government can afford to pay for [the soldiers]."

The jitters of Jakarta's business community highlight just how vulnerable the Indonesian economy has suddenly become. Although President Suharto, 75, has overseen unprecedented

growth over the past three decades, his policies have also ignited popular discontent now bubbling to the surface. Rampant corruption, economic inequality, and political oppression have become flashpoints for disgruntled workers, the urban unemployed, and muzzled intellectuals. All this, plus the lack of a successor to Suharto, is giving pause to domestic and foreign investors. "I think it's almost a certainty that there will be more violence," says a Jakarta-based U.S. telecommunications executive.

VULNERABLE. The key question is whether Indonesia can maintain its current economic growth rate of 7.8% through what promises to be a rocky political period. The financial markets clearly have been shaken. Bomb scares have emptied office buildings that house Chase Manhattan Bank and the state-

DIMMING FUTURE?

A key question is whether Indonesia can maintain its 7.8% growth rate in rocky times

owned Bank Rakyat Indonesia. The rupiah plummeted 1.2% on July 29, to 2,365 against the dollar, a one-year low. Stock prices plunged 6% on July 27 and have yet to fully recover. Jonathan Harris, research director of brokerage PT HG Asia Indonesia, thinks prices will stay jumpy



for months. "The market is definitely concerned," Harris says.

Indonesia is particularly susceptible to financial shocks because of its huge \$90 billion foreign debt. Its current-account deficit in the year ending Mar. 31, 1997, could be about \$8.6 billion, up from \$5 billion. "We are a high-debt country," admits Soedradjad Djiwandono, the go-

INDONESIA'S ECONOMIC PRESSURE POINTS

FINANCIAL MARKETS With a debt of \$100 billion, the country is vulnerable to rescheduling woes.

DIRECT INVESTMENT Major multinational firms could stall fresh outlays, hurting job creation.

LABOR UNREST With workers dissatisfied with low wages, unions are stepping up activism in factories.

CAPITAL FLIGHT Ethnic Chinese, fearing persecution, could move money offshore.

DATA: BUSINESS WEEK





OUTLAWED

Suharto's decision to undermine reformer Megawati triggered violent protests

franchises, petrochemical complexes, and trading monopolies for essential commodities.

Some have rallied around Megawati Sukarnoputri and other reformist leaders of the opposition Indonesian Democratic Party

(PDI). It was Suharto's decision to engineer her ouster as party leader that triggered the violence in the first place. Megawati, the 49-year-old daughter of former President Sukarno, however, is far from a skilled politician, and her political faction lacks organization. Still, she is gaining support from important groups such as labor unions.

"PEOPLE POWER." How these unions respond to the political uncertainty is critical. If most remain docile, it's possible the economy could shrug off much of the strife. But some union leaders sense opportunity and are striving for political power. Take the banned Indonesian Prosperity Trade Union. Led by attorney Muchtar Pakpahan, this union has been waging a crusade to get the government to change 30 labor laws that it believes violate Indonesia's constitution. But the group has gotten nowhere through the ruling party, Golkar, or the legal system. Pakpahan in mid-July said the union would now try to organize a "people power revolution" that he hopes Megawati can lead. "She can articulate the aspirations of the grassroots," he said. Pakpahan was arrested on July 30.

Because he still controls the security apparatus, Suharto seems determined to try riding out the storm. He has yet to rule out running for a sixth term in 1998. He has made it clear he will not brook open elections. What's more, while it is assumed that Suharto's successor will be from the military, a native of the main island of Java, and a Muslim, nobody knows who it will be. Over the years, the President has purged any rising leader who appeared powerful enough to pose a threat.

On the economic front, Suharto seems to be betting that he can retain the confidence of enough financial mavens and corporate investors to maintain growth. That may work for a while. But the riots could prove to be the early tremors of a post-Suharto earthquake if deep-seated problems are left to fester.

By Pete Engardio, with Michael Shari, in Jakarta and Mark Clifford in Hong Kong

nor of Bank Indonesia. "We understand the concerns of foreign investors." Another worry is whether the violence will cause direct foreign investment to drop off. Over the past five years, Indonesia has sucked in more than \$13 billion from U.S., European, and Asian multinationals and oil giants. Those commitments have contributed heavily to its success as an Asian export platform. Although no investors are pulling out, new deals are now being pulled into question as multinationals worry about the reliability of the Indonesian government.

Overseas Chinese investors from Hong Kong, Taiwan, and Singapore must also think twice about their Indonesian strategies. That's because entrenched Indonesians have traditionally focused their frustration by reaching homes and businesses of the ethnic Chinese minority who dominate the economy but represent only a tiny percentage of the population. Overseas Chinese investors have linked up with Indonesian-Chinese companies such as the Salim Group to form major ven-

tures. A branch of Salim's Bank Central Asia was trashed in the riots. If wealthy ethnic Chinese shift their capital offshore, that could have a big impact on the country's financial markets.

To ensure continued prosperity, analysts say, Suharto must address the concerns of Indonesians who haven't benefited from the country's growth. Wilson Nababan, president of the consulting firm P.T. CISI Raya Utama, estimates that 15% of Indonesians, or 30 million people, live in poverty. Despite Jakarta's glistening office towers, American steak houses, and young millionaires, factory wages average \$2 per day, while the average monthly pay for civil servants is less than \$45. "Only a few are getting rich," says H. Aziz Boeang, a university lecturer and opposition supporter.

Many Indonesians are fed up with widespread corruption and nepotism. Most need to pay bribes for a phone line or to register a car. Some anger is directed at the First Family. Suharto's six children have parlayed their connections into business empires valued at an estimated \$4 billion that span rich telecom



CHEONG: The CEO is cutting costs and diversifying with a leasing subsidiary

Until recently, Singapore Airlines Ltd. flight attendants who became pregnant were prohibited from donning the Paris-designed, body-hugging batik sarongs that have made them into international symbols. But now the airline is so desperate for its highly marketed Singapore Girls that for the first time it rehired two dozen flight attendants who had quit to have children. Even when Singapore Airlines offers higher pay, a labor crunch created by the island nation's high growth means "you can't get people," says Deputy Chairman and Chief Executive Officer Cheong Choong Kong.

Singapore Airlines' challenges go a lot further than finding enough crew members to serve the fresh-squeezed orange juice and *premier cru* Bordeaux that have helped it win repeated awards. Like many companies throughout Asia, Singapore Airlines is scrambling to stay competitive as a booming economy soaks up workers and raises costs. More competition is coming from regional rivals such as Malaysian Airlines System, which is expanding and slashing prices. And a strong Singapore dollar is hitting earnings because more than 80% of the airline's revenues are in weakening overseas currencies.

But odds are Southeast Asia's premier airline will manage to muscle through a difficult period by gearing up aggressively at the same time that it slashes costs. An ambitious expansion plan should see its fleet soar from 70 to 150 jets by 2004. Last November, it announced a staggering \$12.7 billion order for up to 77 Boeing 777s. "It's got good management and the cleanest balance sheet in the industry," says Chin Y. Lim, an analyst at Morgan Stanley Asia in Singapore. "It's better placed than any other carrier in the region to withstand competition."

CASH HOARD. How can it find enough flights for all the new jets? The airline figures that much of the new capacity will be soaked up by the 8% to 10% annual growth expected in its Asian routes. "This is going to be where the action is for the next decade," says Cheong. Singapore Airlines' wholly owned Silk Air subsidiary is expected to break into the black this year because of soaring tourism traffic. Analysts say Singapore also may buy

a piece of a second-tier Asian carrier.

The airline believes that growth ways such as these will lead it through its current profit pressures (chart). Although still among the most profitable carriers in the world, Singapore Airlines' earnings fell 5%, to \$622.3 million, in the year ended Mar. 31, because of the stiffer competition and rising costs. But thanks to the Singapore government's 54% stake, Cheong is less worried about quarterly profits than many of his rivals. In fact, he's sitting on nearly \$800 million in cash, a hoard sufficient for future investments. The airline is also unique for its ability to pay cash for most of its airplanes, and virtually free of long-term debt.

These strengths will give Cheong enough time to lower his cost structure. He has already moved data processing operations to Madras, India, in a venture with the Tata group. Cheong has outsourced many of the airline's accounting activities to Beijing, and he figures that the bulk of the routine work now done in Singapore will move to lower-cost countries. Singapore Airlines is also trying to use technology more efficiently to save on labor costs, eliminating boarding passes on many flights, for example.

As a way of escaping the squeeze on its main business, Singapore Airlines is trying to diversify by creating subsidiaries. Part of the record-setting Boeing 777 order is for the company's new leasing subsidiary, aimed at reducing its dependence on sales of its used aircraft. Moreover, it has taken minority stakes in a cargo-handling operation at Hong Kong's new airport and an engineering facility in China.

Singapore Airlines is also likely to make headway outside of Asia despite difficulties in obtaining air rights. Cheong hopes to start service to South America within the next two years, but so far he has not gotten the needed permission from South Africa to allow him to stop en route. The new longer-range planes may help Cheong overcome

some of those problems because he won't need as many refueling stops. And he is optimistic that negotiations will ultimately create freer trade in the skies. "The skies are going to be opened," he says. "It's not a question of whether, but when." Singapore Airlines is betting big that he's right.

By Mark L. Clifford in Singapore

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EUROPE

DOGFIGHT OVER LONDON—AND PARIS, ROME, MADRID...

With full deregulation slated for '97, airlines cut ticket prices

It was an ominous move by Germany's Lufthansa, and a hint of things to come for Europe's other big national airlines. Dogged by feisty new carriers that have slashed fares and taken away passengers, Lufthansa announced on July 29 that it will cut capacity on European routes this fall and launch yet another austerity plan to get costs in line.

Lufthansa's moves are testimony to deep changes that are rapidly altering the competitive scene in European skies. As years of gradual deregulation move toward a final witching hour next Apr. 1—the date when any European Union carrier can fly anywhere in the EU—both new and old airlines are racing to grab or protect market share in advance. And that is putting strong downward pressure on airfares, exactly as deregulators in Brussels hoped.

AMBITIOUS. The fare cutting spells trouble for many of Europe's big airlines. Italy's national carrier, Alitalia, is feeling such pressure from upstart Air One

that it's offering a \$66 fare anywhere in Italy on Tuesdays and Wednesdays in August. Soon, Alitalia will face another ambitious startup, Vicenza-based Alpi Eagles, backed by big industrialists including the Benetton clothing family. "We're going to see a lot of downward movement on prices," says Paolo Rubino, managing director of Rome-based Air One. Experts at American Express Co. figure that prices on some of the major national routes, like Paris-Marseille and Berlin-Munich, will plummet by as much as 33% over the next couple of years. "Consumers are going to save billions of dollars," predicts Bob Har-

rell, a New York-based airline consultant to American Express.

The big carriers are hatching strategies to hang onto traffic. In late July, British Airways PLC increased its stake in the French domestic carrier TAT European Airlines, from 49.9% to 100%. BA is bringing in a new CEO to stem losses and build French feed for the parent's global routes. In response, Air France has been planning to convert its domestic subsidiary, Air Inter, into a new trans-European carrier—Air France Europe—manned by new pilots who would fly much longer hours. But in July, a Paris court ruled that present pilots can't be fired as Air France had planned. The carrier will still start shuttle service this fall between Paris and three provincial cities.

SHIPPING TYCOON. The French carrier is at special risk from a gaggle of scrappy low-cost rivals lining up to steal its markets. One is Air Liberté, a former charter carrier. Chairman Lotfi Belhassine claims that Air Liberté has taken 40% of the Paris-Toulouse market since it won the right to fly inside France two years ago, and a big chunk of Paris-Nice.

Airline entrepreneurs are even more active in Britain. Last November, Stelios Haji-Ioannou, the 29-year-old son of a Greek shipping tycoon, launched Easy Jet with flights between London and Scotland. Modeled on no-frills U.S. airlines, the carrier issues no tickets, bypasses travel agents, and flies from Luton Airport, where landing fees are low. Richard Branson's new no-frills Virgin Express is based on a Brussels startup. Euro Belgian Airlines, that he acquired in April.

If U.S. deregulation is any guide, some of these startups won't survive. Still, "there are a lot of soft markets to attack in Europe," says Keith McMullan, managing director of airline consultant

EUROPE'S FARE-CUTTING UPSTARTS

Low roundtrip fares shake up the European market

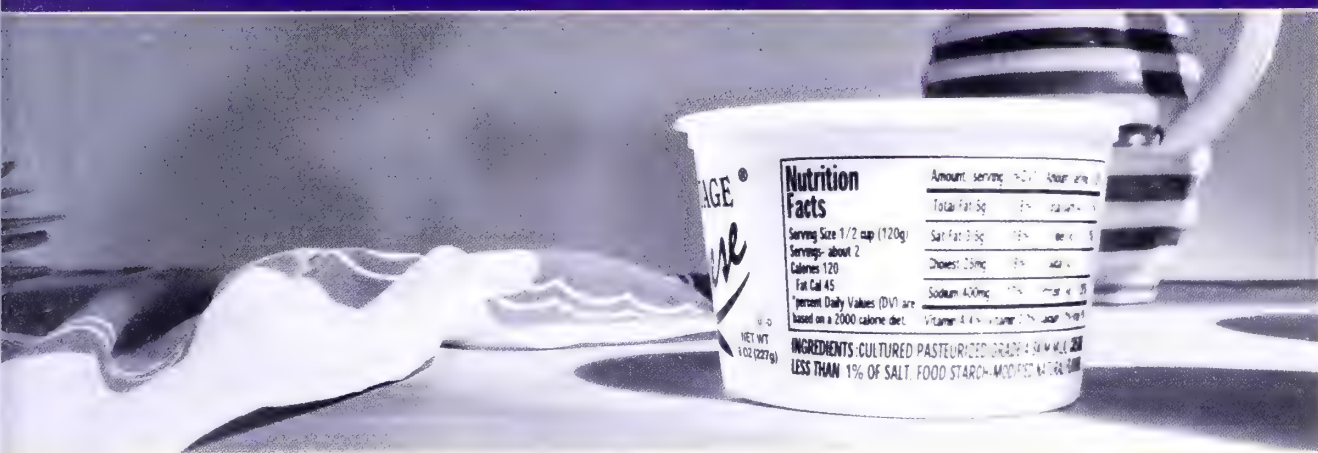


DATA: INDIVIDUAL AIRLINES

Avmark International in London. Come April, those markets will be under stronger attack, and not just by startups but by efficient big carriers such as British Airways. Lufthansa's retrenchment seems sure to have sequels elsewhere, as the battle in Europe's skies grows hotter.

By Stewart Toy
Paris, with bureaur
reports

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BURMESE BEEB: The revered World Service will no longer be separate

BRITAIN

THE BBC AS WE KNOW IT IS SIGNING OFF

New media realities are forcing it to slim down drastically

It's a tricky business trying to change "Auntie." That's the nickname for the 74-year-old British Broadcasting Corp., and it rightly conveys the affection most British have for the publicly funded broadcaster. John Birt, director-general of the BBC, discovered in June how quickly the public would rush to Auntie's aid when he announced dramatic plans to merge the TV and radio operations—including the revered World Service. A roar of protest arose from BBC reporters, ordinary viewers, and government officials, all fearful that the BBC's standards would be hopelessly compromised. One member of Parliament denounced Birt for acting like some tyrannical czar.

Fortunately for Birt, Parliament is going on recess, so the public debate will simmer down a bit. Yet the uproar is sure to resume in the fall. The reason: Birt is contemplating a major transformation of the broadcaster that will cause plenty of pain.

Birt, who is not giving interviews these days, insists this change is necessary. The launch of digital broadcasting services in Britain by Rupert Murdoch's BSkyB is expected to boost the number of TV channels from 30 to 200-plus next year. As a result the Beeb's own forecasts show that audience share for the four traditional channels—BBC 1, BBC 2,

ITV, and Channel 4—will fall to 65% from 90% within 10 years.

Theoretically the BBC is protected from this tumult. Every year the government levies a \$140 fee from every TV-watching household in Britain, for a total of \$2.8 billion. The levy provides a big part of the BBC's \$3.5 billion revenues, with the rest coming from the sale of programming overseas and the BBC's two international television channels. The public has always supported the levy. But as BBC



BIRT'S BBC BLUEPRINT

STREAMLINE THE NEWS

DIVISION Radio and television staffs will be merged into one team, and the World Service will be combined with the domestic news division

CUT COSTS The goal is to cut costs by 15% by streamlining management, opening productions up to bids, and selling assets

GO DIGITAL Digital technology is at the core of plans for a 24-hour news channel, themed subscription channels, and digital radio with CD sound quality

viewership declines, and consumers discover the pleasures of, say, movies on demand from a BSkyB digital channel that support could seriously erode. "The real question for the BBC is: Can it meet these sweeping changes in the broadcasting world?" says Tim Simpson, consultants Arthur D. Little Ltd.

Birt is acting quickly. In May he announced the BBC's own plans to thrive in the new age. He wants to start a 24-hour news channel, as well as channels that expand on what's available from BBC 1 and BBC 2, and channels devoted to such topics as science and drama. New technology will also allow the BBC to offer crisper sound and broadcast on wide-screen TV. These plans will cost hundreds of millions, which leaves Birt in a bind. He has pledged not to increase the license fee to raise money for his new ventures, and government rules restrict the BBC's ability to borrow. The solution is to wring more money out of operations.

TAKING BIDS. Birt, who moved over from London Weekend Television in 1987 and became boss three years ago, has already cut 4,000 from a workforce of 28,000 and realized savings of \$465 million. But he wants an additional 15% savings over five years. So radio and TV production will be combined to streamline management and avoid duplicated efforts. Birt is accelerating an existing plan requiring BBC producers to compete with outside producers for commissions to make shows for the broadcast division. "They are separating out manufacturing from distribution," says Kevin D. Narain, senior manager of the entertainment, media, and communications group at Price Waterhouse. "That makes perfect commercial sense. To raise more funds, the BBC is selling more programming worldwide, such as the *Pride and Prejudice* miniseries.

These ambitions make supporters of the old BBC very uneasy. The rationale for restructuring "is an argument based on accountability, not quality," says Steve Barnett, senior lecturer in media studies at the University of Westminster. Alton Lennon, president of BECTU, the union of BBC producers, says members are already complaining about having cut corners compared to five years ago.

Birt would cause considerable harm if he destroys quality and marginalizes the World Service. But he deserves some sympathy. A media revolution is set to engulf Europe. Somehow the BBC must prepare for it.

By Heidi Dawley in London

Can you spot the 7 ways to catch a virus?

Sales rep picks up notebook computer from MIS department.

Goes to airport.

Flight cancelled. Downloads stock market news from the Internet.

Accesses email.

Catches plane.

Copies game from fellow passenger.

Opens attached document on email from research assistant.

Arrives at regional sales office and loads demo disk for presentation.

Accesses online service for up-to-the-minute industry projections.

Borrows floppy from hotel business office to print presentation.

Arrives at client and begins presentation.

That dreaded message appears: "Application error. Program file corrupted."

Blurts expletive.

Protection

This sales rep encountered 7 computer viruses in just one trip. Think of all the times you run into similar situations in the office, on the road, or even at home with the floppies your kids are borrowing. Yikes.

PROBLEMS:

1. You can catch a virus by using someone else's computer.
2. You can catch viruses off the Internet.
3. Floppies are petri dishes for viruses. If you share games or applications, you could be sharing viruses.
4. Anytime you open an attached email document, you can catch a virus.
5. If you share software, whether it's from a friend or someone at the office, you can get a virus.
6. Even though most online services scan their content for viruses, some viruses slip by and don't show up until the worst possible moment. Then, it's too late. You're infected.
7. Hotel business centers can be breeding grounds for viruses.

SOLUTION:

Norton AntiVirus® protects against the very real threat of computer viruses by automatically detecting and eliminating viruses before they corrupt your system. Installed in minutes, it's the most popular anti-virus program, used by 94% of the Fortune 100 companies.

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LIKE A ROCK



EDITED BY STANLEY REED

A COUPLE OF WINS FOR ZEDILLO— BUT DON'T BREAK OUT THE TEQUILA

At last, Mexican President Ernesto Zedillo Ponce de León can take credit for success. In late July, he got Mexico's three major political parties to agree to a long stalled deal that could finally create a genuine multiparty political system. He also did President Bill Clinton a big favor by paying back \$7 billion owed to the U.S., thanks mainly to a surprising \$6 billion international debt issue. Only \$3.5 billion of the \$12.5 billion Mexico borrowed from the U.S. last year remains outstanding.

The debt payback bolsters Mexico's standing in the international financial markets. At the same time, the electoral pact should ease investors' concerns about political instability. The key feature of the deal takes the federal judiciary, which Zedillo is cleaning up, the final arbiter of election disputes.

But the most important thing about these achievements is that they have made Zedillo seem in charge—after months of being overshadowed by economic crisis and the preceding administration's legacy of scandal.

It is far from clear, however, that the uncharismatic Zedillo can keep the initiative. Political reform could easily bog down as the parties tussle again to hammer out details.

UNTOUCHABLE ISSUES. The economy may be even harder to manage. The government will announce soon that growth is 5% or more in the second quarter. That will be a cue for brokerage houses to declare Mexico's recovery solidly under way. But the celebrations will be premature. It is not a sure thing that Mexico can sustain 5% annual growth. In fact, the apparently strong showing in the second quarter still owe much to the 10.5% drop in the same period in 1995. Most forecasters expect 1996 and 1997 to turn in growth of between 3% and 4%—well below what Mexico

needs to start recouping what it lost in the collapse of 1995.

Most Mexicans are not feeling the recovery, which is largely limited to the export sector, representing about a quarter of the economy. Mexican workers on average have 25% less purchasing power than they did before the devaluation in December, 1994.

With the domestic market still stagnant, foreign investors needed to spur job growth have remained on the sidelines. "Unless you get the investment, you won't get the employment, and you won't get the consumption," warns Shauna de Brun, president of the American Chamber of Commerce of Mexico.

Zedillo is well aware that next year's congressional elections are likely to be a referendum on his management of the economy. So he is feeling pressure to stimulate. He has some room to maneuver without spooking Wall Street because inflation, 1.6% for June, is falling faster than expected. Spending will accelerate in the second half, and the central bank is already easing up on its monetary straitjacket.

But if Zedillo wants to push economic growth any further he'll have

to use his new credibility to back measures that will attract foreign investment. Privatization must move ahead more quickly, especially in the energy sector, and he may have to tackle untouchable issues, such as Mexico's rigid labor code. His government also needs to get credit flowing again through the troubled banking system.

Despite all the obstacles, the outlook is brighter than at any time in Zedillo's so far disastrous term. But the president does not have much margin for error. He has to keep making hits. Otherwise, scandals and other negatives may quickly reconquer the headlines.

By Elisabeth Malkin in Mexico City



THIN WALLETS: Purchasing power is weak

GLOBAL WRAPUP

HONG KONG CELL PHONES

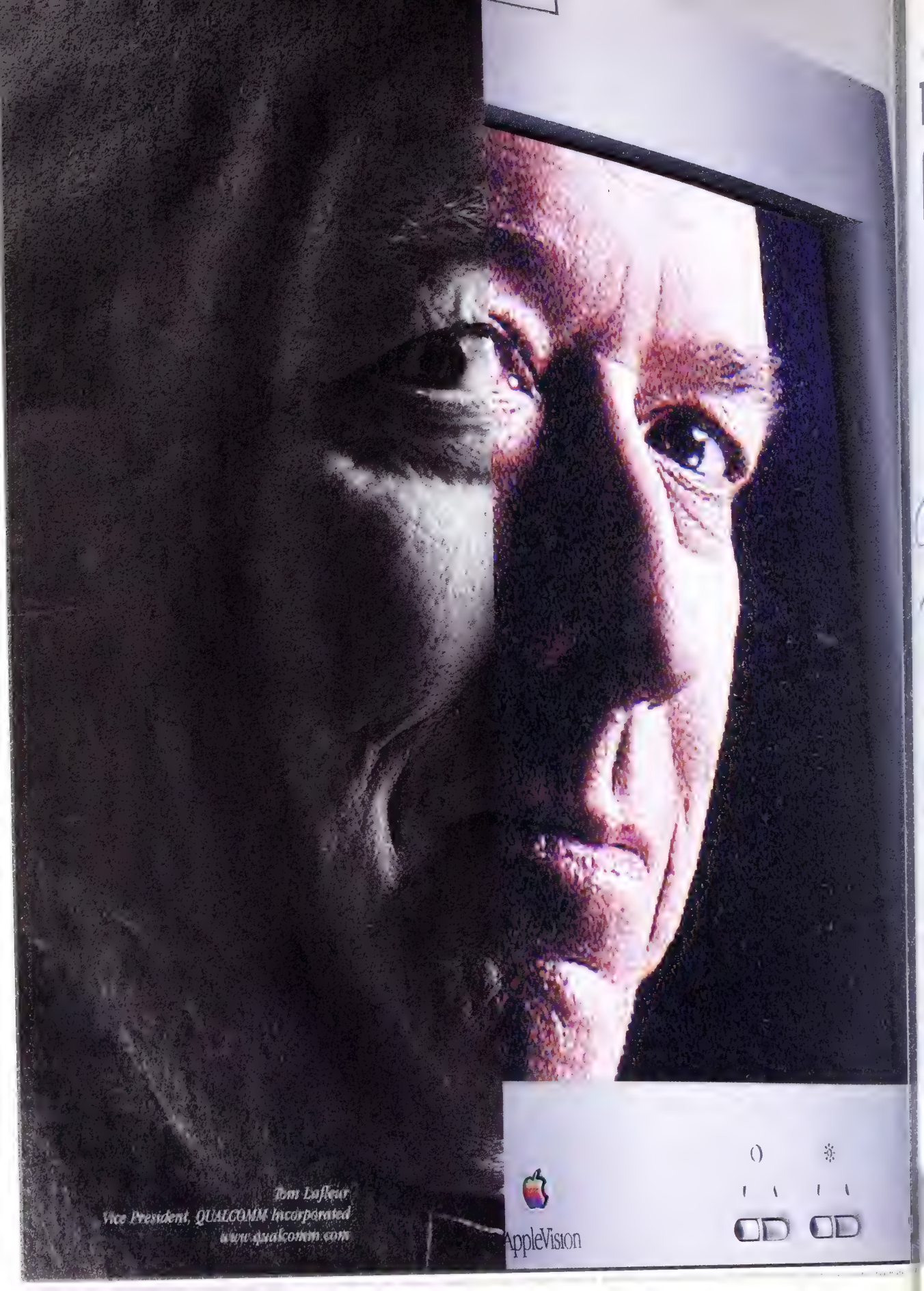
► China has belatedly agreed to allow Hong Kong to issue six new mobile telephone licenses. China's green light is a positive sign for business after next year's transition. Each of the new licensees will have to spend at least \$129 million on their cellular networks, and consumers are expected to benefit from sharply lower prices. Hong Kong is one of the most cellular-crazy markets in the world. Some 14% of the territory's 6 million people subscribe to such services.

The actual awards produced some surprises. Hong Kong Telecom, the colony's dominant provider, failed to secure a license—making it a big loser. Two consortiums, which included Chinese telecom operators, were also shut out. A Taiwan firm, Pacific Wire Electric, is a member of one winning group.

NO SUBSIDIES FOR VW?

► In a move that could eventually cost business billions of dollars in investment inducements, the European Union has ruled that the east German state of Saxony cannot subsidize two

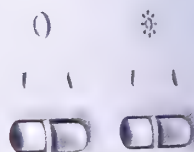
planned Volkswagen manufacturing plants. But Saxony, which is desperate for the 23,000 jobs that the factories would generate, says that it will defy the European Union and proceed with the \$160 million in aid. Bonn will probably side with Brussels, which is worried about overcapacity in the automobile industry. The government of Chancellor Helmut Kohl is trying to head off a subsidy war on the Continent. Both sides say that they will seek arbitration from the Court of Justice of the European Communities in Luxembourg.



Tom LaFleur
Vice President, QUALCOMM Incorporated
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CYBER-MOGUL

To conquer the Net, Masayoshi Son takes to the high wire

At some point amid the endless courses of sashimi, tempura, and chilled octopus, Masayoshi Son's deal-making synapses started firing frantically. Son had invited Rupert Murdoch to a swank Ginza eatery for an evening of *kaiseki ryori*, or Japanese haute cuisine, in late May. Having heard that Murdoch's News Corp. might launch the Japanese equivalent of its British Sky Broadcasting Corp. satellite-TV service, Son grilled the media tycoon. Bemused, Murdoch acknowledged the plan, then mentioned some potential Japanese partners.

As the sake flowed, Son started emoting about his own digital dreams for his Softbank Corp., the software distributor he has built into a high-tech powerhouse. After a \$3 billion, two-year, debt-fueled acquisition tear, Son, the president and CEO of Softbank, already had emerged as the world's biggest computer-trade-show impresario and most powerful publisher of high-tech magazines. Softbank was pumping big money into unproven but promising Internet ventures. Why not jump into the high-tech world of digital broadcasting, too? "I told Rupert, 'The partner you're talking to is all wrong,'" Son says with a laugh. "'It should be me.'"

The next morning, Murdoch summoned Son to the Park Hyatt Tokyo Hotel, and the outlines of a deal started to emerge. On June 20, the duo unveiled plans to pay \$380 million for 21.4% of Asahi National Broadcasting Co. Highly rated Asahi TV would serve as the programming and news-gathering base for Japan Sky Broadcast, their 50-50 venture. Overnight, Son had escorted Murdoch the Barbarian right into the cloistered world of Japanese media.

Crashing the gates and disrupting the old order is standard operating procedure for the 39-year-old Son. In a nation where high tech is dominated by lumbering, tradition-bound

The Softbank Empire

Masayoshi Son has built his software distribution business into a \$2.6 billion, global high-tech powerhouse

PUBLISHING

With its \$2.1 billion acquisition of Ziff-Davis Publishing, Softbank became the world's biggest computer publisher. Ziff, with annual revenues of \$850 million, has 80 print titles, including *PC Magazine*, *Computer Shopper*, *PC Week*, and *Mac Week*. Ziff also publishes more than 200 "how-to" manuals annually. Son's plan is to expand to 1,000 print titles by 2005.



TRADE SHOWS

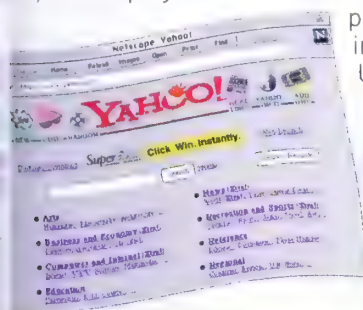
Softbank is now the biggest computer trade show organizer in the world, with a 75% lock on the lucrative U.S. market. Through its 1995 acquisition of Interface Group, Son took over Comdex, the industry's biggest virtual



INTERNET

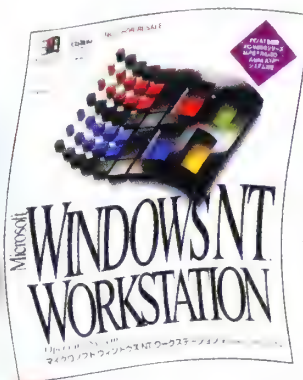
Softbank has spent \$200 million snapping up stakes in some 30 Internet startups including Yahoo!, CyberCash Inc., and inquiry.com. Softbank Interactive is also a big

player in Web advertising with 40% of the U.S. market.



SOFTWARE DISTRIBUTION

Softbank, a wholesale distributor, controls more than 40% of Japan's software market. Softbank distributes 30% of Microsoft's programs in Japan and has teamed up with the software giant to develop PC game software.



MULTIMEDIA PROGRAMMING

A joint venture with Nippon Telegraph & Telephone, plans to distribute digital movies and software to Japanese homes via phone line. And, together with Rupert Murdoch, Son bought 21.4% of TV network Asahi National Broadcasting, with an eye toward launching a satellite-TV service in Japan. In the U.S., a Ziff unit is creating *The Site*, a daily computer show for the MSNBC cable network.

NETWORKING

Softbank owns 20.4% of Novell Japan Ltd., the coming subsidiary of the p network software supplier. An alliance with Cisco Systems is aimed at promoting a Japanese standard for network equipment.



electronics conglomerates, Son stands out as a Western-style entrepreneur, part Bill Gates, part Murdoch. He's a nonstop networker and dealmaker whose circle includes such Silicon Valley luminaries as Oracle Chairman Lawrence Ellison, Sun Microsystems CEO Scott McNealy, and Microsoft's Gates, a frequent golfing buddy.

Since Softbank, Son's confederation of high-tech publishing, trade-show, distribution, and software companies, went public in 1994, its stock has soared 200%, to \$160, adjusted for three splits. Son's 52% stake, worth \$4.5 billion, makes him one of Japan's wealthiest businessmen. Even with the stock off over 20% from its high, Softbank trades at 150 times

last year's earnings.

It commands this lofty valuation because Son's ambitions—if realized—will make Softbank a huge force in high-tech marketing in the 21st century. Already a massive marketing machine in Japan, Softbank is branching out—into the U.S. and onto the Internet.

Through a combination of print publications, TV programs, trade shows, and online services, Son is positioning Softbank to be everywhere consumers and businesses buy, sell, or talk about information technology.

RIPE PLUM. In other words, Son's empire could become the hub of a massive digital marketplace. Advertising alone—in magazines and Web sites that cater to computer shoppers—will grow from last year's \$2.2 billion to \$4.7 billion in 2000, according to New York-based media consultants Wilkofsky Gruen Associates. But there's a bigger plum. That's to get in the middle of the transactions that move hundreds of billions worth of personal computing products every year. In Japan, Softbank already does that through its wholesale business. Now, as more and more technology products are flogged in cyberspace, Son sees a way to get a cut of the business in the U.S. and around the world. "The Internet is where our future is," he says.

To get ready, Son has been using his richly valued stock—and a staggering \$2.4 billion of debt—to assemble an international network of companies. In 1994, he bought Ziff-Davis

Publishing Co.'s computer trade-show business for \$202 million. Last year, he paid \$800 million for the Interface Group, which runs Comdex, the computer industry's biggest show. With those buys, Son got 75% of the U.S. computer trade-show business. Then, in February, he paid a stunning \$2.1 billion for Ziff-Davis Publishing, the \$850 million-a-year computer publisher. Among Ziff's 30 titles are the three biggest in the field: *PC Magazine*, *Computer Shopper*, and *PC Week*.

He's not stopping there. Softbank is now on the verge of a \$1 billion acquisition aimed at further strengthening its position in the U.S. Company officials won't say what kind of

As an ethnic Korean, Son grew up belonging to a despised

company Son is after. But, says Gary Reischel, senior vice-president of the U.S. affiliate Softbank Holdings Inc., "this is a big play in one of our core businesses."

Where will Son's empire-building end? "I have a 300-year plan for ourselves," he says without a hint of irony. Meeting with Ziff-Davis employees, Son was asked if the Ziff deal would be his crowning achievement. His reply was that Ziff is important, but just one step in his personal 50-year plan. "I want to do something really big in my 40s," Son told the stunned employees.

DEEP POCKETS? There are questions, however, as to whether Softbank can keep up with the boss's ambitions. Up to this point, Son has been able to fund his drive into the U.S. by exploiting favorable currency exchange rates and Softbank's surging stock price. But he's saddled with an awesome \$2.4 billion in debt and mounting interest payments. Some Tokyo analysts are concerned that the company is already stretched thin. But Chief Financial Officer Yoshitaka Kitao figures that with Japan's low interest rates, Softbank could easily handle \$3 billion more in acquisitions. He cites another development that cuts his costs and also indicates confidence in Softbank: Its bond rating has been upgraded from BBB+ to A-.

So far, Son has been able to go after just about whatever catches his eye. Since early 1995, he and his scouts at Ziff have scoured Silicon Valley for promising Internet startups (table, page 59). Through two company-controlled venture-capital funds and Softbank itself, Son has put more than \$200 million into some 30 Net companies, including Yahoo!, the top World Wide Web search-engine service. Son's 37% stake was worth \$200 million after the initial public offering in April, but has since fallen to about \$65 million.

Son wants more than a quick buck, though. He sees synergy between investments like Yahoo! and other Softbank businesses. The Yahoo! site is one of the best advertising venues on the Net. Also, Son has launched a Japanese-language version of Yahoo!. In turn, it has become a major client of Cyber Communications Inc., a joint online advertising venture between Softbank and ad giant Dentsu Inc.

Another example of Net synergy is the investment in

U.S. Web, which helps companies set up online storefronts. It will sell content from Ziff-Davis and advertising services from Softbank Interactive, too. Internet Profile Corp., in which Son has about a 10% stake, counts the number of visits made to Web sites—a Nielsen-like service that will help Softbank sell online ads.

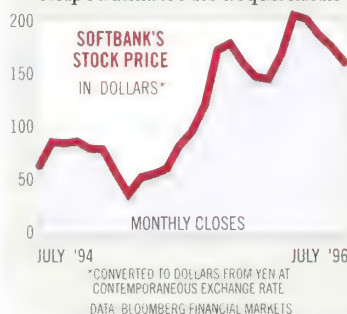
When Son sees a company with promise, he pounces. He decided to back Yahoo! over pizza with its founders. After a preliminary feeler via E-mail, he met with CyberCash Chairman Dan Lynch last spring at a lounge in San Francisco International Airport. They cut a deal for Softbank to pay \$15.4 million for a 9.5% stake. "It took about an hour," marvels Lynch.

Son has now raised a separate \$500 million Internet venture fund backed by Asian investors. So confident is he in his investment acumen that he has pledged \$500 million of his own to guarantee investors' principal. Oh yes, he also will take a 5% management fee and 35% of the capital gain. Most venture funds keep 25%.

When he's done, Son expects to have a network of companies that will work in concert to create a new digital ma-

BUYING POWER

Softbank's lofty stock price has helped finance its acquisitions



Son's Big Dare

Foreign investors aren't enchanted with his risky plays

► **ACCOUNTING** Softbank is writing off \$2.7 billion in goodwill over a 30-year period from his Ziff-Davis and Comdex buyouts rather than the more conventional 10 to 15. So instead of a \$270 million charge against earnings, Softbank is taking only \$90 million a year. That allowed it to report a net profit of \$132 million in 1995, instead of barely turning a profit.

► **STOCK AS CHEAP MONEY** Softbank has raised \$630 million in fresh equity to finance its spending spree. So far, the dilution hasn't hurt investors. But that could change when \$640 million in convertible bonds come due over 5 years. Softbank's stock has already fallen 20% from its high, reducing Son's buying power.

► **LEVERAGE** Son's \$3 billion spending spree on U.S. assets has saddled Softbank with \$2.4 billion in debt—more than twice its equity level. With 70% of its pre-tax earnings now coming from the mature Comdex and Ziff-Davis buyouts, Son can't afford to misstep.

► **CURRENCY RISK** Son bought Comdex and Ziff-Davis when the yen soared. Now the yen has weakened. That cuts his buying power even as it boosts earnings. Some 25% of Softbank's earnings in fiscal 1995 came from currency gains.

GAMBLING CFO

Yoshitaka Kitao engineered Son's debt-heavy strategy

minority. Still an outsider, he makes up his own rules

etplace. Having built his fortune partly by using his Japanese computer magazines to plug the products that Softbank sells, Son sees endless possibilities for cross-promotion on the Net. The Web's hyperlinking technology nicely blurs the lines between editorial content and advertising, making it easy to lead a consumer from a product review to a vendor ad to an online store—with Softbank collecting a fee at every stop. The pieces are falling into place. Shortly after Son acquired Ziff-Davis, for instance, it recast its startup publication *Internet Life* as *Yahoo! Internet Life* to focus on the Son affiliate. And on May 9, Son snapped up 20% of inquiry.com, which provides information on high-tech products and companies on its Web site—a natural promotional vehicle.

OTHER LODGE. Son also plans to cull a huge direct-marketing database from the 9 million Ziff-Davis subscribers and trade-show attendees. He hopes to share the data, including who owns what type of computers and software, among Softbank companies and affiliates and sell it to others. "This is an incredible marketing tool," says Son.

By yearend, Softbank plans to have a Web site linking all its businesses. Then, a Net surfer visiting a Ziff magazine site will be able to link to another page to learn more about an upcoming Comdex event, or visit a Softbank online store for a software download. Softbank's first online shop, Net-buyer, will be launched by ZDnet this fall. Son says that 50% of Softbank profits will be Net-generated in five years and 50% in 10 years.

If he can get through the next few years, that is. Son's amazing buying streak has been fueled by some lucky breaks and some energetic financial engineering. Softbank bought In-Place, for example, when a supercharged yen was around 80 to the dollar. Now, with the yen at 109, Softbank has lucked out again: Its earnings are getting an extra kick as U.S. prof-

its are converted to yen. A quarter of Softbank's earnings last year were currency-driven.

But exchange rates could swing against Son, and with its huge debt load, Softbank could soon see its earnings growth stall. To pay for Ziff, for example, Son raised \$630 million in cash from an equity offering but borrowed the rest with convertible and straight bonds. Softbank's \$2.4 billion in debt is more than twice its equity. Interest expenses will jump from \$3.4 million in fiscal 1995 to an estimated \$82 million in fiscal 1996, ending next March. So far, growth has kept Softbank from feeling the pinch. Pretax earnings tripled, to \$132 million, in fiscal 1995, and analysts expect a 66% gain this year, to \$220 million on \$2.6 billion in revenues.

Maintaining a high stock price is another key to Son's buying plans, and that may become trickier. Some analysts have already soured on Softbank stock, in part because of aggressive accounting practices that reduce the impact of the buying binge on earnings. Softbank decided to write off \$2.7 billion in goodwill from the Ziff-Davis and Comdex buyouts over 30 years rather than the more conventional 10 to 15 years. "If they wrote off the goodwill over 10 years, they would barely be profitable," figures Jonathan Dobson, a fund manager with Jardine Fleming Investment Management's OTC Fund. Last month, he dumped his \$30 million stake, about 5% of his total Japan holdings. Softbank insists that its accounting is prudent given the brand value and market-leading positions of the properties.

Concern about possible dilution in Softbank shares also has scared off foreign investors, Dobson says. Foreigners own just 4% of Softbank shares vs. 20% at other fast-growth

Cover Story

Seeding the Future

Where Son has bet \$200 million on the Internet

► WEB SERVICES / ADVERTISING

Andromedia
Decisive Technology
Electric Classifieds
E*Trade Group
I/Pro (Interactive Profiles)
Multex
Softbank Interactive Marketing
USWeb
Yahoo!

► ONLINE PUBLISHING

2Way Media
inquiry.com

► ELECTRONIC COMMERCE

CyberCash
Electric Communities

► GAMES

Engage Games
Express Plus
GT Interactive Software
Kinesoft Development
SEGA Entertainment

► WEB SOFTWARE

Agents
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BACKWEB
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Freeloader
Intervista Software
IOTA
OnLive! Technologies



Japanese companies, he notes. The reason: \$640 million in convertible bonds will turn into new shares over the next five years.

Then there are questions about how well the Softbank's cross-selling will work in the U.S. While Ziff employees insist there has been no pressure to compromise editorial integrity—by emphasizing companies or products that Softbank has interests in, for example—rivals suggest that Softbank inevitably will abuse its power. One fear is that Softbank could trade coveted Comdex booth positions for more ads from computer makers. "They are positioning the business more toward a selling system and away from an independent journalistic enterprise or exposition field," says Patrick J. McGovern, chairman of International Data Group (box). Counters Son: "We have a very neutral position on editorial content."

"DARKNESS INSIDE." Son didn't get where he is by paying attention to such qualms. The grandson of Korean immigrants, he has spent his life making his own rules to get around barriers. He has succeeded, but the pain of growing up as a member of a despised minority has never gone away. The out-

PROWLING COMDEX

Son relentlessly chases deals, and his buying streak isn't over yet



AND IN THIS CORNER, PAT MCGOVERN

Patrick J. McGovern already had built a modest fortune from publishing computer trade magazines and was dabbling in venture capital in 1981 when he came across Masayoshi Son. The young entrepreneur was trying to launch a software-distribution business out of a cramped Tokyo office furnished with a couple of crates. Son struck McGovern as a kindred spirit, but the American figured Japan wasn't ready for an "energetic chap" like Son and passed on the chance to back the startup.

Fifteen years later, Son's Softbank Corp. has emerged as the biggest and best-financed competitor to McGovern's Boston-based International Data Group. Their rivalry, which includes trade shows and market research (Softbank's Ziff-Davis unit owns Computer Intelligence Inc.) is most visible in the battle for readers and advertisers in the computer press. Son's Ziff-Davis Publishing Co. gets 39% of the ad revenues in the market, and IDG grabs 27% through *Computerworld*, *InfoWorld*, and 285 other titles.

It's an interesting matchup. The two are opposites in many ways. While Son is outgoing, McGovern is reserved. Son has dealt his way into the big leagues by loading up on debt and issuing equi-

ty, while McGovern has kept IDG private, funding new ventures with retained earnings. McGovern, 58, still owns 63% of the company he founded in 1964; a generous employee stock ownership plan owns 35%. He claims he has no debt and \$150 million in the bank.

Instead of buying assets, McGovern has pursued global expansion, starting with international editions of his publications, from *ComputerWorld Pakistan* to *PC World Myanmar*. IDG is now the largest foreign publisher in China. Since 1990, overseas forays have helped IDG grow from \$550 million to \$1.4 billion in annual revenues, says McGovern.

Another hot growth area has been the ...for *Dummies* series, which began with *DOS for Dummies* in 1992 and now includes guides on everything from personal finance to sex. *Dummies* sales hit \$112 million last year. IDG's trade-show business took in \$126 million, and market researcher International Data Corp. added \$130 million.

NOT RATTLED. Back when Son and many of today's other techno-visionaries were in diapers, McGovern grasped that computers would be a world-shaping force. As a biophysics student at Massachusetts Institute of Technology in the 1950s, McGovern earned pocket money

writing and editing for *Computer Automation*, an early computer magazine. He stayed on after graduation became associate publisher.

The IDG empire got its start a few years later after a computer executive complained to him about the lack of solid information about customers in the new market. McGovern formed IDG and began gathering data on users' terms and product preferences. In 1978, he launched *ComputerWorld*, a magazine aimed at corporate computer buyers. After 12 months, the publication went from 16 to 72 pages.

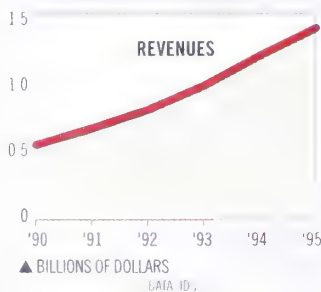
Both McGovern and Son see the Internet as their next battlefield. But while Son believes advertising will be his biggest moneymaker online, McGovern's plan is to charge subscription fees for Web sites and rake off a royalty of 10% on any sales they generate. While most of the \$20 million IDG took in last year from online ventures came from ads, McGovern is convinced in the long term, user fees will be where the money is. IDG's three Web-only publications: *JavaWorld*, *Netscape World*, and *SunWorld*, carry subscription prices of \$9.95 a month and together total 85,000 subscribers.

McGovern says he is not rattled

THE NEW GOLD RUSH

McGovern's rivalry with Son has segued from the computer press to the Net's myriad untapped vei-

IDG'S GLOBAL PUSH IS FUELING GROWTH



ardly exuberant Son calls this pain his "darkness inside." Born in Tosu on the island of Kyushu, Son was given the panese surname Yasumoto because of a Japanese law aimed forcing assimilation. That didn't stop racism, however. When I was in kindergarten, some kid hit me in the head th a stone," Son recalls. "It hurt me emotionally, and I ded to try to hide my identity."

At 16, Son bolted to South San Francisco where he lived th family friends. He assumed his Korean name, Jung-eui n and, after high school, enrolled at the University of Calrnia at Berkeley. An economics major, he made a small forne importing the Space Invaders video game from Japan. e also co-developed an electronic dictionary that he later d to Sharp Corp.

After Berkeley, Son returned to Japan and in 1981 nched Softbank. He saw two opportunities: to distribute ware to Japan's consumer electronics and computer stores d to fill the need for readable high-tech magazines.

So he went looking for a bank loan, using his Korean surme. After so many years in the U.S., he was shocked by e rejections that followed. But instead of retreating, this e he persisted. He recalls that when skeptical loan officers ould suggest Son was a strange name, he would snap,

of the high-profile Softbank "It hasn't affected the pace of e're doing," he says. While Son spending hundreds of millions investments and generating profits from online ventures in e, McGovern is sticking to his d-true pattern. IDG spent \$40 o fund online ventures in the e years and will spend another

\$40 million over the next three. McGovern's modest goal is for Web publishing to bring in 15% of revenues by 2000.

Still, McGovern may have to do more than stick with his success formula. With Softbank expanding on all fronts, International Data Group could find itself surrounded.

By Paul C. Judge in Boston



"O.K., I'm a Korean, so what?" Eventually, a sympathetic banker at Dai-Ichi Kangyo Bank Ltd. relented with a \$1 million loan. "I told him he could use my life as the collateral," Son jokes.

It was a bumpy start. Son would rent out booths at trade shows and phone software companies offering to display their titles for free. But manufacturers ignored him and went right to the retailers. The big break came when Osaka-based Joshin Denki Co. asked Son to supply a large quantity of software for a PC superstore it was opening. Son got an exclusive deal by offering every major software package in Japan. It took inspired salesmanship to persuade software makers to go along, but it worked.

His business almost collapsed in the mid-1980s, however, when a scandal at Dai-Ichi forced the bankers to call in risky loans such as Son's. Desperate, he received emergency financing from Industrial Bank of Japan. Then came another setback. He was hospitalized in 1984 with hepatitis and was forced to give up day-to-day control. "The company tried to keep it very secret," recalls Novell Japan President Kazuya Watanabe, a Son friend for 10 years. "Yet everybody knew he had great difficulties."

On the mend by 1987, Son resumed control, and Softbank started to get a dominant share of the software-distribution market. The near-collapse of Ascii Corp., Microsoft's original distributor, helped. So did key alliances. Son helped set up the Japanese subsidiary of network software supplier Novell Inc.—taking a 25% stake (now 20.4%). Another joint venture, Softbank Korea was formed with Pohang Iron & Steel Co. Some ventures didn't pan out, though. Softbank dropped \$10 million in a botched online shopping venture, and an attempt to distribute dozens of software programs on a single CD-ROM flopped.

Now, Softbank has taken off, along with the Japanese PC market, where shipments jumped 70% last year. Softbank moves 30% of Microsoft's Windows 95 and Word programs in Japan, as well as 15% of Novell software. And it distributes 60,000 other software titles and a variety of PC gear. Revenue is expected to hit \$2.6 billion this year—up from \$408 million in 1990.

HARD KNOCKS. Son has now joined the ranks of the superrich. But he scarcely hides his disdain for the old-boy network that would not let a Korean in. "I'm maybe the fourth-richest guy in Japan—and the other three probably inherited real estate from their fathers," he says.

Within his business empire, Son has also busted the Japanese management mold. Instead of the usual pyramid, Softbank is run as a network of 64 profit centers. During Son's illness, he began decentralizing, organizing his workers into groups of 10, each with profit-loss statements that would be updated daily. Those who ran out of cash ran out of luck. Today, top executives meet with Son for biannual "1,000 knocks" sessions—grueling five-hour meetings in which the boss scrutinizes every detail of business plans. "Son likes measuring everything," explains Softbank Holdings' Reis-

Cover Story

Cover Story



chel, "and taking a stick and tapping something 1,000 times."

On the other hand, Son also doles out lavish bonuses to star performers. Last year, he gave \$1 million to Softbank's managing director of networking and \$500,000 to the editor-in-chief of the magazine that covers DOS/V, the Japanese-language version of the MS-DOS operating system.

Outside Softbank, Son is known as a charming schmoozer—and a relentless deal-chaser. Take the Ziff-Davis saga. After negotiating licensing deals to publish Japanese versions of Ziff computer magazines, Son cultivated social ties with the reclusive Ziff family. Eric Hippeau, Ziff's chairman and CEO, recalls the time when Son, along with his wife and two young daughters, visited William B. Ziff Jr. at his retreat in Aspen, Colo. When Ziff suggested a hot-air balloon ride, Son didn't hesitate. The Sons set out in one balloon and Hippeau and some other Ziff execs were in another. As they floated around, Hippeau began to wonder why he didn't see Son in the other balloon. It was not until they landed that the diminutive Son came crawling out of the balloon's basket and confided that heights made him queasy.

When the Ziff family decided to sell out in 1994, Son thought he might have the inside track. Instead, he was blindsided when they canceled an auction and sold 94% of the company to buyout boutique Forstmann Little & Co. for \$1.4 billion. Forstmann offered an all-cash bid that was lower than Son's \$1.6 billion offer. Son might have won it had his Japanese banks moved faster. "Forstmann had the cash in hand," says Softbank CFO Kitao, a Cambridge-educated ex-Nomura Securities Co. man whom Son hired after the debacle.

BLUE PERIOD. Son went home with the consolation prize, Ziff's trade shows. But he didn't give up. He kept pressing Theodore J. Forstmann, who refused to see him, sending "not for sale" messages via underlings. Last fall, Forstmann relented. Son, Kitao, and Forstmann's team met at the financier's Park Avenue apartment. As they admired the Picassos and Matises, the deal talk began. The next day, Softbank agreed to pay a whopping \$2.1 billion for Ziff, handing Forstmann a \$700 million profit.

The price stunned media analysts who said Son overpaid for a mature franchise. Computer makers were shifting ad dollars

FLYING SOLO

Son rejects the consensus-seeking, centralized Japan Inc. style of management

to TV and general-interest publications such as *Time*. Ziff, they figured, was most vulnerable since *PC Magazine*, *PC Week*, and *Computer Shopper* deliver 80% of its profits.

Again, Son lucked out. Driven by the Net, PC ads are growing twice as fast as other print ads. Ziff magazine revenue rose a healthy 9.8% in 1996's first half, according to Adscope Inc., despite ad pages at *PC Magazine* being off 2%.

Now, Son has a bold plan for Ziff: to go from 80 print titles now to 1,000 in 10 years. That means adding almost two titles a week. It's not as crazy as it sounds. Ziff has lots of opportunities to expand internationally. It already licenses its 30 U.S. publications in 100 countries, but most countries carry only one or two titles. Softbank is also adding to Ziff through startups and acquisitions, most recently buying Chicago-based Sendai Publishing Group and its magazines about computer games.

Increasingly, though, Son is interested in electronic media. He has plowed \$20 million into a TV venture, including a studio in San Francisco where ZD-TV will produce shows that promote high-tech products. The first show is *The Site*, which is carried on the new MSNBC cable-TV network. Murdoch's Hong Kong-based STAR-TV will carry Ziff's programming in Asia. Ziff also is exploring radio over the Net.

Softbank is also betting big on cyber advertising. Online ads are a \$50 million market now, but some analysts predict they could hit \$2 billion in four years. Softbank Interactive, created by merging Interactive Marketing Inc. with Softbank's Internet sales division, already places 40% of the ads in cyberspace. ZDnet itself is one of the top sites for ad revenues.

All of these ventures could indeed have the vast potential Son foresees. But it's hard to ignore the financial high-wire act needed to keep his enterprises going. Son, characteristically, seems unconcerned. He keeps a grueling schedule, crossing the Pacific two or three times a month. At the Comdex gathering in May, Son cruised the floor with Ziff editors, looking for Internet investments. In a T-shirt and V-neck sweater, he looked like a Silicon Valley guy. And he acted like a kid in a candy store. This cyber mogul had arrived.

By Brian Bremner in Tokyo, with Amy Cortez in New York and bureau reports



Travel Tools



Travel Cars



Travel Hotels

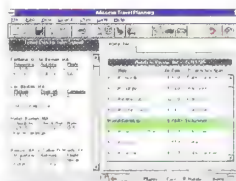
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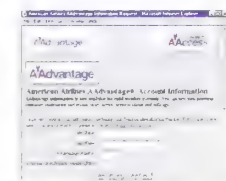
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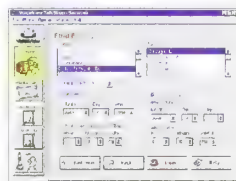
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HORSE RACING

THE HORSE BIZ SHOWS A LITTLE LATHER

It ain't the '80s, but Thoroughbreds are out of the dog days

Electricity was in the warm air of the Keeneland yearling auction on July 15-16 in Lexington, Ky., with millionaire breeders sharing knowing smiles. As the average price for Kentucky's most prized Thoroughbreds jumped to a six-year high amid predictions of a resurgence in the long-beleaguered industry, tuxedoed auctioneer Tom Caldwell sealed a one million-dollar bid by giddily blurted out what many others were no doubt thinking: "This is almost like the '80s, isn't it?"

Well, not quite. True, the \$349,880 average sale price marks an unexpectedly vigorous 41.6% increase over 1995. But it's far from the halcyon days of the '80s, when favorable tax laws stoked a speculative fever that lured many novices to invest and drove the average Thoroughbred price to more than a half-million dollars by the middle of the decade. "In those days, people bought horses like stocks," says Irish breeder John Magnier. The resulting glut of horseflesh and the Tax Reform Act of 1986 sent the market into a wrenching contraction. The bankrupt Calumet Farm went from a symbol of Kentucky's horse-racing tradition to a symbol of the industry's malaise.

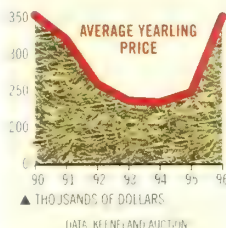
SUPPLY AND DEMAND. While the prices of the '80s are unlikely to be seen again anytime soon, many say the industry is back—healthier and well-positioned for sustainable growth. The downturn drove most of the speculators out of the market, says David L. Switzer, executive director of the Kentucky Thoroughbred Racing Assn., adding: "Today, we're playing with real dollars."

Another reason for the recent uptick

is the relative dearth of quality horses. The supply-demand curve has finally turned in the breeders' favor. Even though the number of horses going under the hammer at Keeneland dropped from 188 a year ago to 167, the gross jumped more than 25%, from \$46.4 million to \$58.4 million. Four horses topped the \$1 million mark—the most since 1991—including sale champ Storm Cat, at \$1.7 million. "More money chasing fewer horses is a sign of strength [in the indus-



THE PRICE OF A PONY REARS UP



"I'VE GOT A HORSE RIGHT HERE": Storm Cat went for \$1.7 mil

try]," says Henryk De Kwiatkowski, the Polish-born entrepreneur who became a Bluegrass hero by saving Calumet from shopping-mall developers.

Even more significant is the trend toward globalization. The U.S. horse-racing market reached maturity years ago, and competition from other forms of gambling are slowly whittling away at its base. However, elsewhere in the world, especially in Asia and the Persian Gulf, the sport is wildly popular, and purses dwarf those of America. So demand outside the U.S. for racing and breeding stock keeps rising.

Japanese investors, who spent near one-third of the dollars dropped at Keeneland, have become the most important new component in the U.S. market. Until recently, Japanese racing was restricted to domestic equine. But relaxed rules and tired bloodlines have the Japanese flocking to Lexington. "The best stock comes from Kentucky, so we come to Kentucky," says Tony Yoshida, who represents various Japanese interests.

While the Japanese emerge as key players in the comeback of the American Thoroughbred market, some Kentucky breeders see a worrisome parallel between today and the years after World War II. For generations, British blood stock was considered the world's best, but Americans invested heavily and were able to supplant the Brits. "They're taking our blood, and I worry about the day that [the Japanese] don't have to come back," says Robert Clay

whose Three Chimneys Farm in Lexington is home to Triple Crown winner Seattle Slew.

The exporting of Kentucky blood may be troubling to some, but breeders are clearly pinning their hopes on overseas markets. New tracks and breeding farms are springing up around the world, particularly in South America, China, and Eastern Europe. "Eastern Europe is the next wave," predicts Dan Kwiatkowski. "In time, they will be a factor [in the Kentucky sales]."

Japanese, Eastern Europeans. Surprisingly, they're all increasingly important to the Thoroughbred industry. But romance and status are still what make the sport of kings run. Breeders talk at events about "selling dreams," and only in Kentucky are the dreams so fraught with history and the blood of champions. Says CEO Fusao Sekiguchi of Japanese Meitec Corp., who spent \$5.75 million on seven yearlings: "Racing gives romance to the man, it gives dreams to the man." And spenders like Sekiguchi give hope to America's horse business.

By Keith Dunnivant
Lexington, Ky.

e also helped
ild the path
at leads to it.



For many U.S. athletes, the journey to the medal ceremony passes through Colorado Springs. That's home to the U.S. Olympic Committee and one of three U.S. Olympic Training Centers. Recently, this high-altitude training ground added impressive new dining, housing, medical and visitors' facilities — built, in part, through donations of our plywood, lumber, CraftMaster® door facings, Nevamar® laminates and Fountainhead® solid surfacing. So while we're proud to have the athletes stand on platforms made from our wood during the 1996 Summer Games, we're especially proud to support that other "Olympic Village" — the U.S. Olympic Training Center — 1,400 miles west.

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THE FIRE THIS TIME

Cigarette makers now face FDA oversight

The next battle in the tobacco wars is about to erupt. Any day now, the Food & Drug Administration is expected to rein in the tobacco industry by asserting jurisdiction over cigarettes and other products. Sources say the new rules will mirror regulations the agency originally proposed last August. The goal: to slash smoking by adolescents in half within seven years by eliminating vending machines, billboard advertising, and many forms of promotion aimed at youths. If it goes forward, FDA officials believe, the plan could eventually whittle down the nation's annual \$50 billion medical bill from tobacco-related illnesses by preventing teenagers from getting hooked in the first place.

Powerful political winds are gusting up behind the proposal. As the Presidential race heats up, tobacco regulation is turning into a campaign issue. When Bob Dole casually suggested in June that nicotine was not addictive and that the FDA should just butt out, gleeful Democrats quickly trotted out ads saying that Dole is standing idle while 3,000 kids a day start a habit that will kill one-third of them. "If Dole loses, a lot of it could be his statement on tobacco," frets Representative Linda Smith (R-Wash.).

Indeed, public outrage at Big Tobacco appears to be rising.

According to a new *Charlotte Observer*/WSOC-TV poll, 48% of voters even in tobacco-growing South Carolina favor FDA regulation. Adding to the momentum, plaintiffs' lawyers and journalists have recently unearthed several documents indicating the industry targets underage smokers. One

1973 R.J. Reynolds Tobacco memo, for instance, discusses marketing to the "'21 and under' group." A company spokesperson says the document is a draft and that none of its proposals were adopted.

TWISTING ARMS. But this pro-regulatory juggernaut is heading toward an industry primed for war. Although the expected regulations themselves won't have much of an economic impact on tobacco, the industry wants no part of FDA control. Tobacco executives claim—despite repeated assurances to the contrary by agency chief David A. Kessler—that the current plan is merely a first step to much tighter constraints. Tobacco will never be able to meet the FDA legal requirement for medical devices of being "safe," admits Tobacco Institute spokesman Thomas Lauria. So "if it asserts jurisdiction, the FDA would be breaking the law if didn't ban tobacco," he says. "FDA regulation is tantamount to putting

the tobacco industry out of business.

So Big Tobacco is mounting an extensive counterattack (table). Last August, five companies filed suit in federal court in North Carolina claiming that the FDA has no legal basis for regulating tobacco. Since then, lobbyists have been arm-twisting in Congress, where 82% of members have taken industry money, to keep the FDA from issuing final rules. And once regulations are issued, manufacturers will immediately go to court to seek an injunction. Promises Charles A. Blixt, vice-president and general counsel of RJR.

Even though the industry claims that the FDA proposal is a matter of life and death, the actual restriction on manufacturers would be "pretty benign," says Roy L. Burry, tobacco analyst at Oppenheimer & Co. They are expected to include bans on vending machines, mail order sales, free samples, self-service displays, and such non-tobacco items as hats emblazoned with



NOT WAITING TO INHALE: 3,000 kids a day get started

Big Tobacco vs. the FDA

The agency wants to regulate tobacco to cut youth smoking, but the industry is fighting back with a variety of tactics

BLOCK THE REGULATIONS Industry lobbyists are trying to convince legislators to halt the FDA move. So far, little success.

COMPROMISE Two companies have proposed federal legislation, agreeing to many of the restrictions, in exchange for the FDA not asserting jurisdiction. No lawmakers have yet taken up their cause in Congress.

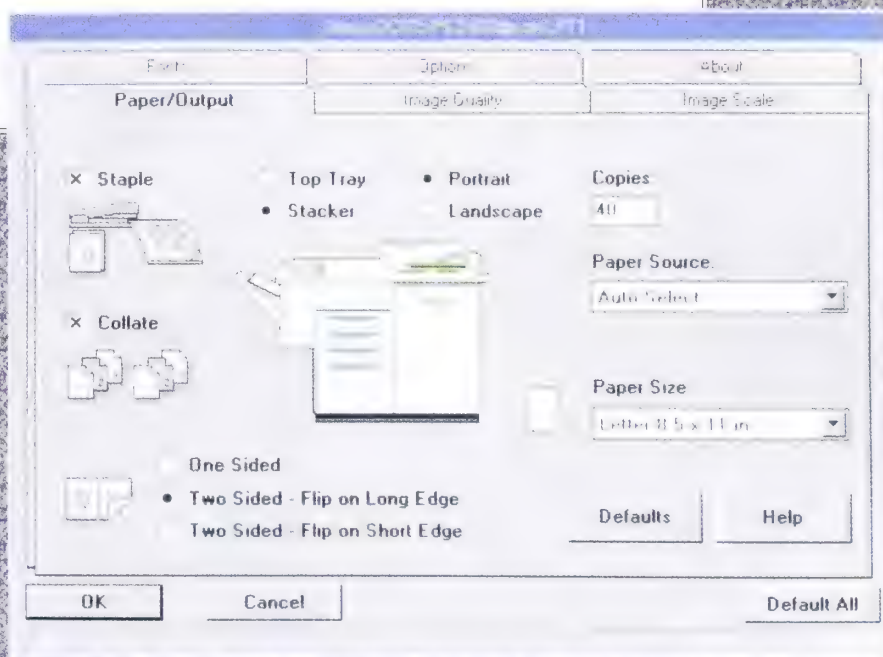
SUE Manufacturers have taken the FDA to court, arguing that it has no legal authority to regulate tobacco. A recent Supreme Court decision may have fortified their case.



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brand names. They would also ban photos and illustrations from ads in publications popular with kids and prohibit the use of brand names as sponsors of events such as rodeos, allowing corporate backing only. If the FDA implements all of last August's proposals, companies would also have to kick in \$150 million total for an antismoking campaign for kids.

None of these rules will take a big swipe out of revenues, predict analysts. The youth market accounts for only 3.5% of the \$45 billion to \$50 billion in domestic sales each year. And even if the rules do cut smoking, the U.S. market will probably shrink by only 2% a year, predicts Ronald Thomas, vice-president at ASB Capital Management Inc. "That's a drop in the bucket," he says.

FRIENDLY CAMEL. The lack of significant economic impact may be one reason Philip Morris Cos. and U.S. Tobacco Co. proposed their own legislative plan in May. The companies' deal: If Congress would agree to bar the FDA from regulating tobacco, they would agree to many of the specific restrictions the agency is seeking. But the cigarette manufacturers have not found a lawmaker bold (or stupid) enough to introduce its scheme in Congress. And while other tobacco companies are considering similar deals, the industry can't agree on one common proposal. For instance, RJR does not support its competitors' proposed advertising restrictions. "We need to compete for those people who chose to smoke and try to get them to smoke our brands," explains Blixt.

Because the industry clearly cannot count on a congressional bailout, Blixt believes that manufacturers' best hopes lie in the North Carolina federal suit. Their odds of success appear to have improved in May, when the U.S. Supreme Court ruled that the Constitution prohibits Rhode Island from banning price information in alcohol ads. Some legal experts say the major free-speech decision may bar the FDA's proposed advertising restrictions. But agency officials respond that the high court's 44 *Liquormart Inc. vs. Rhode Island* decision is not relevant. They claim that the ruling only applies to factual information, not promotional images, such as Joe Camel, that could be misleading, making tobacco seem safer than dangerous.

It's too early to know whether the industry will win in court. But with antitobacco forces gaining strength, companies may not be able to stave off government controls for long.

By John Carey in Washington, with Lori Bongiorno and Mike France in New York

The Workplace

EMPLOYEE OWNERSHIP

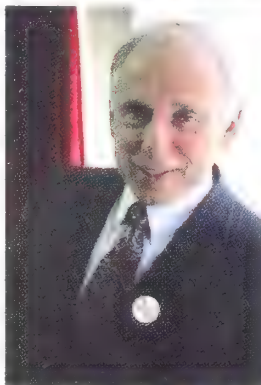
SHOULD AVIS TRY HARDER —FOR ITS EMPLOYEES?

Critics say a proposed sale could shortchange worker-owners

For the past nine years, Avis CEO Joseph V. Vittoria has won plenty of plaudits for the Employee Stock Ownership Plan (ESOP) that he helped to set up at the No. 2 car-rental agency. Under his guidance, Avis Inc. has been a prominent example of employee ownership and has pushed the image of a company run by highly motivated employee-owners. Vittoria himself has been a poster boy for the concept, landing a plum position last year as a board member representing salaried employees at United Air Lines Inc., the country's largest ESOP.

Now Vittoria and the Avis experiment are coming under harsh scrutiny. In early July, management announced a tentative agreement to sell the company to HFS Inc., the nation's largest hotel franchiser, for \$763 million. Employees, who own 71% of Avis, won't vote on the deal until they receive a proxy in late August. But as the terms become public, ESOP experts are asking whether employees are getting shortchanged by their co-owners, which include Vittoria and other managers, and General Motors Corp., which owns 29% of Avis.

A WARNING. The proposed sale calls for 10,000 U.S. employees to get \$356 million, while Vittoria and other managers would make \$157 million and GM \$250 million. But employees should be taking home some \$500 million, argues Malon Wilkus, president of American Capital Strategies Ltd., a Bethesda (Md.) com-



LINE OF FIRE

Employees (above) protesting the terms of the sale to HFS at Avis' Garden City (N.Y.) offices; CEO Vittoria insists the deal is fair, but some experts say he has favored his own interests over the ESOP's

pany that helps unions set up ESOPs. He has been retained by the Teamsters union, which represents a fifth of Avis employees. "This deal is unfair to employees and illegal" under federal pension law, charges Wilkus. On July 31, the union sent a letter to the ESOP trustee Charles E. Wert, an executive vice-president of U.S. Trust Co. of California, demanding that the deal be renegotiated. It also is mulling a lawsuit or a proxy battle urging employees to vote down the deal. Vittoria denies that the transaction is unfair to employees, as does Wert. "We have fully carried out our fiduciary responsibility to employees," says Wert.

Whatever happens with the proposed buyout deal, it stands as a warning about the potential misuse of employee

membership. Where there are aggressive labor unions in ESOP companies, such as those at United, they often safeguard employee interests. But most of the country's 9,000 ESOPs involve private, often small, companies that typically have no employee group. That leaves management with enormous latitude to structure an ESOP pretty much as it sees fit. And because management often prescribes the trustees that are required by federal law to oversee ESOPs for employees, the trustees frequently rubber-stamp management, experts say. The current deal at Avis "points up the need for more shareholder rights for employees, to be certain that the interests of management and employees are dealt with separately," says Joseph R. Blasi, a management professor and ESOP expert at Rutgers University.

Indeed, the proposed sale to HFS does raise questions. The deal calls for HFS, a private company based in Parsippany, N.J., that owns Days Inn, Howard Johnson, and six other hotel chains, to buy Avis for \$400 million in cash, \$360 million in HFS stock, and the assumption of \$2.2 billion in Avis debt.

FAVORABLE TAX BREAKS. The key to how employees' shares are valued—the lightning-rod issue—centers on this debt. When the ESOP was set up in 1987, Avis borrowed about \$1 billion for the purchase of a fleet of cars. To take advantage of a lower tax rate for ESOPs, this debt was rolled into the ESOP, along with an additional \$750 million the plan borrowed to buy the company, says Vittoria. The ESOP then functioned like any other. It sold employees' 71% ownership stake in Avis, releasing shares to employees each year as Avis paid down the debt. Because the plan has only paid off \$750 million so far, employees will have been allocated some 9.7 million shares when the HFS deal closes. The remaining 13.9 million remain in the ESOP trust account.

Vittoria contends that employees only own the 9.7 million shares. The unallocated shares still in the ESOP aren't worth anything close to \$1 billion, argues Vittoria and the trustee. So employees will get nothing for these shares, which they must surrender to HFS to pay for the \$1 billion debt. Vittoria and the trustee have told employees that they're nonetheless getting a good deal, since their \$356 million works out to \$36.63 a share on the 9.7 million allocated shares. By contrast, GM would get \$24.42 a share. And about 200 Avis managers would get \$25 to \$36.63 a share for their ownership interests.

Critics see the deal differently. They argue that the ESOP holds the \$1 billion in debt because Vittoria and the trustee involved in 1987 chose to set it that way for tax purposes, a point

Vittoria concedes. But ESOP experts contend that all of the company's owners, including management and GM, benefited from the tax break. So why aren't they equally responsible for paying off the ESOP debt? Indeed, Avis—not the ESOP—has borrowed \$1.2 billion more to buy vehicles since 1987, which HFS also would assume as part of the sale. "The \$1 billion isn't really ESOP debt. It's debt of the company," says Adam D. Chinn, a partner and ESOP expert at Wachtell, Lipton, Rosen & Katz.

Employees aren't getting a fair shake

\$15.28 a share, far less than GM and management (table). A fair deal, says Wilkus, would give employees some \$500 million, vs. the \$356 million they stand to earn now.

The Teamsters and outside experts complain that Vittoria has favored his own interests ahead of the ESOP's all along. He and other managers still hold \$72 million worth of preferred shares that pay annual dividends of 10.25%, according to Vittoria. The company, whose 12-person board is dominated by Vittoria and seven Avis executives, never bought

AVIS SALE: WILL EMPLOYEES COME OUT NO. 3?

WESRAY AND AVIS MANAGEMENT
BUY AVIS INC.

EMPLOYEES

MANAGEMENT

1987

Employee Stock Ownership Plan set up. Borrows \$750 million to buy 100% of company. To exploit ESOP's favorable tax status, it borrows another \$1 billion to pay off existing fleet debt.

Wesray and Avis management retain preferred stock and warrants.

1987 to 1996 ESOP trust, diluted to 71% in 1989, allocates shares to employees as debt is repaid. By 1996, \$750 million of debt is paid off and 41% of the plan's 23.6 million shares are released to employees.

1989 GM buys out Wesray for \$135 million, gaining a 29% stake. Avis issues phantom stock and stock-appreciation rights to management.

1996

HFS Inc. wins a tentative agreement to buy Avis Inc. for \$763 million. But there is a dispute over how to value employees' shares. Avis management and the ESOP trustee argue that the ESOP's remaining \$1 billion in debt renders employees' 13.9 million unallocated shares worthless. Employee bankers say that unallocated shares should not be used to repay the debt because the company as a whole is responsible.

EMPLOYEES

AVIS MANAGEMENT

GENERAL MOTORS

PROCEEDS FROM
PROPOSED SALE

\$356
million

\$157
million

\$250
million

ESTIMATED VALUE
PER SHARE

UNION SAYS
\$15*

MGMT SAYS
\$36**

\$25-\$36

\$24

*ASSUMES EMPLOYEES OWN ALL 23.6 MILLION SHARES IN THE ESOP
DATA: AVIS INC., BUSINESS WEEK

**ASSUMES EMPLOYEES OWN ONLY 9.7 MILLION SHARES

even if they do bear all responsibility for the debt, argues Wilkus, the union's banker. That's because the ESOP's 71% stake entitles the plan to use Avis' cash flow to pay off all the debt it borrowed. Technically, this claim is an asset, asserts Wilkus, that is equal to the value of the debt. "The trustee is breaching his fiduciary responsibility by giving away \$1 billion in ESOP assets," he says. The Labor Dept., which enforces federal pension law, declines to comment, as does HFS. GM says that employees got a fair deal. Wert, the trustee, agrees with Vittoria that Wilkus is wrong and that the ESOP's claim on Avis is worth nowhere near \$1 billion.

If employees do own all 23.6 million shares, the buyout will give them just

out these shares when interest rates fell, even though the company—and the ESOP—would have benefited. Avis couldn't afford to, says Vittoria, who also sat on the ESOP advisory board with two Avis executives until the HFS talks began. Now, the HFS sale will give management back its entire \$72 million.

The rest of management's \$157 million take comes from phantom stock and stock-appreciation rights Avis granted them. While Vittoria won't disclose his share of the \$157 million, it's the "biggest chunk," he says. "That's how life works in these circles." HFS also will keep him on as Avis' CEO and pay him market rates. Whatever Avis' future, privately held ESOPs bear a lot more scrutiny.

By Aaron Bernstein in New York

CAN CADBURY DODGE BIG COLA'S BULLETS?

Coke and Pepsi have put new muscle behind their noncolas



If ever there were a bigger-is-better business, it's soft drinks. In the selling of sweetened fizzy water, a bigger market share equals more advertising clout, stronger bottlers, and better distribution—all of which usually equals still more market share. And as London-based Cadbury Schweppes PLC is learning after spending 10 years and \$3.3 billion to reach the No. 3 position in the U.S. soft-drink market, that means No. 3 isn't a very nice place to be.

Cadbury's biggest push came last year, when it spent \$2.5 billion to buy Dr. Pepper/Seven Up Cos. in an effort to become the premier non-cola soft-drink maker in the U.S. In the mid-1980s, the century-old chocolate company, with 1995 revenues of \$7.4 billion, began a U.S. shopping spree, snapping up such brands as A&W Root Beer, Sunkist, and Canada Dry. Today an estimated 35% of Cadbury's total earnings and 21% of sales come from U.S. beverages. But its 47% share of the U.S. non-cola market translates into only 16.3%

of the U.S. soft-drink market as a whole, and therein lies a problem.

Cadbury got a solid product with Dr. Pepper, the most popular noncola soft drink in the world. Last year, the U.S. market share of Dr. Pepper and its diet and caffeine-free versions rose from 7% to 7.3%, and the brand accounted for 45% of Cadbury's overall U.S. beverage volume. With the Dr. Pepper acquisition, earnings at Cadbury's Americas beverage unit jumped 139% last year, to \$379 million on sales of \$1.7 billion.

But much of Cadbury's lineup is

flat—and facing a competitive onslaught: With the noncola market growing faster than cola, both PepsiCo Inc. and Coca-Cola Co. are moving aggressively into the sector, purchasing root beer brands and other noncola drinks and unleashing big marketing campaigns. Coca-Cola has also renewed its focus on Sprite—at the expense of 7UP (box). To better compete, the company announced on July 29 a reorganization of its North American beverage unit. “We knew by acquiring Dr. Pepper/Seven Up that we would not be below the radar screen of Coke and Pepsi,” says John F. Brock, 48, CEO of Dr. Pepper/Seven Up.

PATCHWORK. Perhaps Cadbury's biggest handicap is its distribution system. Unlike its giant rivals, which have assembled networks of closely affiliated bottlers, Cadbury's soft drinks are distributed by a patchwork of independents—plus a group of bottlers linked to its arch rivals, Coke and Pepsi. With their distribution clout, those Coke and Pepsi bottlers are v

WEAK LINKS

Many Cadbury bottlers are Coke or Pepsi affiliates. One has already dumped A&W Root Beer for Coke's Barq's

tal to Cadbury. But Cadbury's interests often clash with the agendas of those bottlers.

A case in point: Last April, Coca-Cola Enterprises, the world's largest Coke bottler, dumped A&W, Sunkist and Welch's in certain markets in favor of competing Coke brands such as Barq's root beer and Minute Maid. It may be no coincidence that CCE is 45% owned by Coca-Cola. “Coke has drawn a line in the sand and said, ‘We don't want you to compete with us openly,’” says Tom Pirko, managing director of New York consulting firm Bevmark. Analysts say the CCE defection alone could trim 1% from Cadbury's total U.S. earnings.

It wasn't a total betrayal. Cadbury did stick with Dr. Pepper and some of the other brands, ink deals believed to extend for three to five years in certain markets. And so it goes: Coke bottlers keep the strong brand, Dr. Pepper, and other bottlers complain that they're offered only the laggard. And in a market so dominated by the top brands, it's a constant

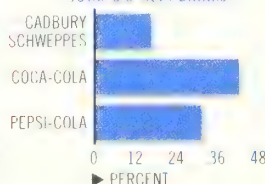
CADBURY IS BIG IN NONCOLAS...

1995 MARKET SHARE
U.S. NONCOLA SOFT DRINKS



...BUT A DISTANT NO. 3 OVERALL

1995 MARKET SHARE
TOTAL U.S. SOFT DRINKS



DATA: WHEAT FIRST BUTCHER SINGER

uggle to get even second-tier offerings o stores. "The reality today," says orge Kalil, president of Kalil Bottling . in Tucson, an independent bottler, that Coca-Cola and Pepsi lock many our brands off the shelves."

In an effort to sort out its distribu- n problems, Cadbury is reorganiz- its North American beverage unit. It will split the company into two op- ing units. Dr Pepper Co. will deal h bottlers carrying the star brand— marily the Coke- and Pepsi-affiliated verhouses. Cadbury Beverages/Sev- Up will work with independent bot- ers that don't carry Dr Pepper.

SPORT SYSTEM. The idea is that h group of bottlers will get coddled a unit that focuses exclusively on t group. The company has set up a port staff to consult with the bot- ers and is working on a program to p them buy more vending machines l refrigerated cases. The indepen- ts say such moves are overdue. hat I want to see is some long-term ement and stability in their man- ement," says William A. Brown,

president of Brown Bottling Group in Jackson, Miss., which distributes Cad- bury products in most of Mississippi.

Cadbury's big shareholders also hope the plan will put some fizz back into the North American beverage operations. "Hopefully, they will be a little more fo- cused [following the restructuring]," says Barbara Trebbi of Ivy Management in Boca Raton, Fla., an institutional in- vestor holding Cadbury's American De- positary Receipts and regular shares. Those ADRs have dropped about 2% this year, to 31%, while Coke's and Pepsi's stocks have posted double-digit gains.

Still, it's unclear how much extra con- trol Cadbury can gain from the changes. "There's no such thing as a level playing field in the soft-drink industry," says Kalil. "When you're not Coca-Cola or PepsiCo, you can't miss a single trick." Some think that means Brock must shoot for more than his stated goal of 50% of the noncola market by 2000 if he wants real clout in the U.S.

With \$1 billion coming Cadbury's way this month from the sale of its 51% stake in British bottler Coca-Cola &

Schweppes Beverages Ltd. to CCE, there are rumors floating around the industry that Cadbury might buy Snapple, the ailing fruit-drink and iced-tea maker now owned by Quaker Oats Co.—or, conversely, that it might sell off some of its smaller brands and focus exclusively on Dr Pepper and 7UP. Most experts believe a bid for Snapple would be a costly distraction. "I think Cadbury's got enough on its plate without taking on what is clearly an enormous turn- around situation," says Julian R.M. Hardwick, an analyst at London-based BZW, an investment bank. Brock says he can't comment on market rumors.

Can Cadbury put more sparkle in its future? It's tough when such a key part of the company's fate isn't entire- ly in its own hands. "Cadbury needs to convince people that they are able to ensure their route to market," says Hardwick, "irrespective of what Coke and Pepsi may decide." Talk about a pressure buildup.

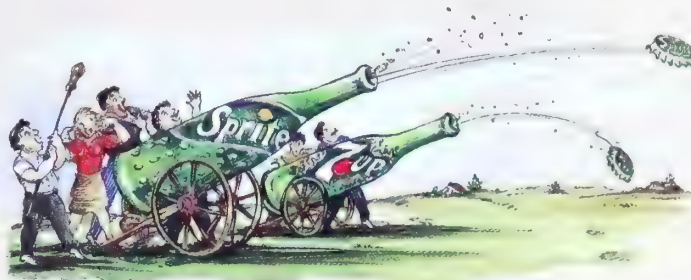
By Susan Jackson in Stamford, Conn., with Stephanie Anderson Forest in Dal- las and Lori Bongiorno in New York

7UP BEHIND THE EIGHT BALL

Whenver 12-year- old Joan Collier sees a Sprite ad on TV, she turns up the volume. Her eyes brighten at the sight of NBA star Grant Hill. But when she sees a 7UP commercial, she's confused: "They keep saying, 'It's an up thing,' but what does that mean?"

Collier's inability to connect is a good example of the problems facing Cadbury Schweppes PLC, maker of 7UP, as it fights an intense uncola war against Coca-Cola Co., which makes Sprite. Since paying \$2.5 billion for the struggling brand and Dr Pepper in 1995, Cadbury has been unable to stop 7UP's slide. In 1985, 7UP held 4% of the soft-drink market, vs. Sprite's 3.8%. Last year, it held 2.8%, while Sprite had 4.9%, according to *Beverage Digest*. Sprite is the fastest-growing of all soft-drink brands in the \$50 billion U.S. market.

For a time, few paid attention to lemon-lime drinks. Before Cadbury bought 7UP, the soft-drink brand had languished for years under a collec- tion of owners. Analysts called the



drink "the orphan." Even Coke nodded off on the category, allowing flavored teas and fruit-based drinks to make a splash. "We created Sprite as a filler, and we didn't promote it right," admits M. Douglas Ivester, Coke's president and coo.

After the acquisition, Cadbury vowed 7UP "would not just be another crayon in the box," says Ian Parmiter, 7UP category vice-presi- dent. Cadbury's first move was to drop the Uncola logo. In a \$25 mil- lion campaign launched in February, Cadbury increased its TV time, changed the packaging, and devel- oped the jingle "It's an up thing."

But the 7UP effort comes almost three years after Coca-Cola began to focus on Sprite, making it the official soft drink of the National Basketball Assn. in the 1993-94 season. Last

year, Coke spending on Sprite increased 54%, to an estimated \$50 mil- lion, according to *Com- petitive Media Report- ing*. One reason Coke is winning is sheer muscle. 7UP is virtually absent from soda fountains at national restaurant chains. And while only about 6% of 7UP's vol- ume is distributed by Coke bottlers,

some of them, such as Charles F. Stephenson, president of Coca-Cola Bottling Group Southwest Inc., are dumping 7UP for Sprite. "It's not showing anywhere near the same growth," says Stephenson.

Cadbury distributes 61% of its 7UP volume through some 140 inde- pendent bottlers who have the loyal- ty but not the bucks to back it up. Still, Cadbury's North American bev- erages chief, John F. Brock, says he's happy with the 7UP plan and its 1% volume growth in the first half of '96. "The 7UP revitalization is off to a solid start," he says. "Sprite is huge, and we expected that." With such a foe, it's far from clear that 7UP will be an up thing for Cadbury.

By Nicole Harris in Atlanta, with Susan Jackson in Stamford, Conn.

PANIC IN THE YEAR ZERO ZERO

Can the financial world reprogram its computers in time?

It's 11:59 p.m. on Friday, Dec. 31, 1999. As the ball drops in Times Square, computers at some of the world's financial institutions shut down. With their lifeblood cut off, these banks, brokerages, and insurance companies, most of which operate in a limited way over the weekend, are forced to close their doors, at least temporarily. Other financial firms whose computers are still functional try to keep operating. But because linkages among financial institutions are so elaborate, even healthy companies begin to falter. By Monday morning, billions of dollars in transactions have been disrupted or aborted. A domino effect goes into play, and in the ensuing confusion the entire financial world teeters into chaos.

The pitch for a Hollywood blockbuster? No, it's the daytime nightmare of one of the most technologically advanced and well-managed firms on Wall Street, Morgan Stanley & Co. It is deeply worried that the computers that keep the financial world alive have not been properly programmed to make the transition to the next millennium.

"IN DENIAL." Wall Street is just one of many industries facing the "Year 2000" problem, which has been getting some press lately. The inability of many computer programs to make accurate calculations after Dec. 31, 1999, will affect everything from the Internal Revenue Service to computer-operated elevators.

The world of finance, though, is especially vulnerable. "Because of the interconnectedness of worldwide financial institutions, the absolute worst case, albeit highly unlikely, is a global financial meltdown," says Kevin E. Parker, Morgan Stanley's head of information technology. Says William Bautz, senior vice-president for technology at the New York Stock Exchange: "Due to the unique nature of this business, everybody has to have the problem fixed, or they create problems for somebody else."

If the specter of financial chaos isn't enough, plaintiffs' lawyers are already viewing securities firms as juicy targets

for a year 2000 litigation bonanza. Investors could sue their brokerage firms over failed trades, unpaid interest, or bad investment decisions caused by incorrect date-based calculations. Law firms are looking into holding boards of directors liable, says Kevin Schick, research director at Gartner Group Inc.

Yet despite the risks, the securities industry has been slow to respond, in part because they are not anxious to spend the estimated \$4 billion it will cost to become year 2000-compliant. "Here is an industry that prides itself on risk assessment and management," says Schick. "And yet, when faced with this potential crisis, they are in denial."

The problem began some 30 years ago. Because of the limited memory space of early computers, programmers didn't want to squander four digits writing out, say, 1962. So they designed software to store dates using only a year's last two digits. The conventional wisdom was that programs would be replaced before 2000 rolled around. But many are still in use. So when 1999 turns to 2000, many computer programs will go from 99, or 1999, to 00—or 1900.

If left uncorrected, this will throw

HOW YEAR 2000 PROBLEMS COULD HURT INVESTORS

- Clearing and settlement of transactions could break down
- Stocks held electronically and checking accounts could be wiped out
- Customers might be denied access to their accounts
- Deposits or trades might not be credited to an account, and customers' funds would not be available
- Interest might not be properly credited to accounts



the financial world into convulsions like it has never seen, say Morgan Stanley computer whizzes. That's because it threatens the underpinning of all financial transactions: the accurate recording of time. The markets are utterly dependent on dates. There are trade dates, maturity dates, settlement dates, record dates, ex-dividend dates, and payable dates, to name a few.

If these dates get screwed up, Wall Street firms' computers will no longer accurately calculate any number of things, says Michael B. Tiernan, a vice president at CS First Boston. He is also chairman of the Securities Industry Assn.'s Year 2000 subcommittee, and testified at congressional hearings in April. Clearing and settlement of transactions could break down. Stocks held electronically and checking accounts could be wiped out. Interest might not be properly credited to accounts. Customers might be denied access to their accounts. Deposits or trades might not be credited to an account, and customers' funds would not be available. "If year 2000 problems are not addressed, the consequences may be catastrophic, from a business and economic



2000 TEAM: Kamen, Parker, and Levine say revising Morgan Stanley's old code will cost tens of millions.

Chairman Arthur Levitt Jr. to sound the alarm. Sources at the meeting with Rubin say he was surprised and sobered. "It is viewed as a technology issue," says LaRoche. "But this is a settlement, counterparty, and systemic financial risk problem." She is referring to huge risks that could be created if millions of transactions between thousands of institutions could not be promptly completed.

Despite these alarms, many institutions are reluctant to make a big investment to solve the problem. "Here we're spending tens of millions of dollars, and it's not going toward anything productive or improving our competitive position," says Parker. Firms that spend the necessary money get to stay in business. And some of those are plotting to take advantage of their competitors' possible demise, says Schick. "We have players looking forward to the great market crash of zero zero," he says. He thinks as firms run out of time to fix their 2000 problems, they will discontinue certain lines of business or even fail.

Of course, not everyone is as apocalyptic as Schick and Morgan Stanley. Renée Nalitt, one of Chase Manhattan's main year 2000 techies, says: "For the most part, we're already in pretty good shape." Securities & Exchange Commissioner Steven M.H. Wallman does not believe the year 2000 presents systemic financial risks and says the issues

spective," Tiernan testified. And there's a further complication: 2000 is a leap year, which means computers may assume there is a Feb. 29.

Yet common reactions are: The computer geeks can fix it, or it can't really be as serious as all that. Schick estimates that only 20% of the industry is in action. Very few securities firms have done audits of their computer programs, the first step toward getting a handle on their situation, he says.

In fact, fixing the problem is far more consuming than might be imagined. Most of the older programs used by all of the financial firms must be revised many times. Morgan Stanley alone is spending tens of millions to change 3 million lines of code. "It's ugly. You have to inventory every single piece of code and manually fix it," says Parker. Programming work must be done on the weekends, since most of the programs are in use during the week. There are only 179 weekends left until Dec. 31, 1999. "You can't do it on the weekend of the greatest party of the millennium," says Joshua S. Levine, a Morgan Stanley managing director whose office overlooks Times Square. "The sand

"Because of the interconnectedness of worldwide financial institutions, the absolute worst case . . . is a global financial meltdown." — KEVIN PARKER, Morgan Stanley

is running out of the hourglass."

Morgan Stanley plans to complete the job well before Jan. 1, 1999. Then the firm will spend 1999 evaluating the efforts of its thousands of counterparties in correcting their year 2000 problems and deciding who to stop doing business with. "We can't assume the risk of being caught in a domino effect," says Morgan Stanley Managing Director Eric M. Kamen.

OVERBLOWN? The white shoe firm is also trying to get other financial institutions and U.S. government regulators to focus on the problem. In June, Elaine LaRoche, a managing director at Morgan Stanley and president of the Public Securities Assn., had meetings with Treasury Secretary Robert E. Rubin and Securities & Exchange Commission

are being addressed responsibly. George Muñoz, a Treasury Dept. assistant secretary who heads a year 2000 Interagency Task Force, says Treasury will be ready by yearend 1998.

The NYSE and Securities Industry Automation Corp., its trade-processing arm, predicts the transition will be seamless. Why? In June, 1996, the industry went from processing trades in five days to three days, a potential back-office disaster that went without a hitch. "There is no chance of the industry not making the changes that are necessary in time," says Michael Reddy, who heads the securities industry year 2000 unit of EDS Corp. He could be right. But if he's not, the next century will start with an unwelcome financial bang.

By Leah Nathans Spiro in New York

MUTUAL FUNDS

'IT'S NICE TO HAVE THIS STUFF IN YOUR BLOOD'

Can Sandy Weill's daughter pep up Smith Barney's mutual funds?

Until 1993, Smith Barney Inc. was a faint blip on the mutual-fund industry radar screen. For all its haughty advertising about making money the old-fashioned way, the prestigious Wall Street firm was well behind its peers, with just \$9.7 billion in fund assets and an embarrassing shortage of top-performing funds.

Then Jessica M. Bibliowicz, at that stage a 34-year-old marketing whiz, showed up. In 1994, she left the top sales post at Prudential Securities' mutual-fund subsidiary and took the job of rebuilding Smith Barney's funds, just after its merger with Shearson Lehman Brothers. Now managing \$74 billion in assets and the nation's ninth-largest fund group, Bibliowicz is turning a laggard into a tough competitor. Her goal? To become the sixth-largest fund company within three years, with more than \$100 billion in assets. "The incredible power of this company has not yet been tapped," she says.

She faces an uphill battle: Most brokerages have been losing mutual-fund market share for a decade. But she has a solid track record—and numerous fans, including her father, Sanford I. Weill, the chief executive of Smith Barney's parent company, Travelers Group Inc. "She'll never get the label off her back" that she's Sandy Weill's daughter, says Michael Downey, her former boss at Prudential. But "it's obvious she didn't get that job just because of her father.... She's a terrific motivational leader."

"TOURIST ATTRACTION." One of two Weill children at Travelers—her older brother Marc is chief investment officer—Bibliowicz was brought up in the world of investing. "It's nice to have this stuff in your blood," she says. She started out as a sales representative at

American Express Co. in 1981, avoiding working directly for Weill until joining Smith Barney in 1994. "I wanted to prove myself without my father's help," she says. When she came to Smith Barney, some employees were skeptical, but attendance went up at staff meetings. "I was the tourist attraction," Bibliowicz says. Personable, articulate, and strong-willed—just like her father—she and Weill are close. Bibliowicz says her fa-



ther dotes on her children, 7 and 5. But at work, she respects the chain of command, reporting to Smith Barney Chief Executive James Dimon.

As a key player in one of the fund industry's biggest gambles, her toughest test is yet to come. Earlier this month, Smith Barney began selling 2,700 no-load funds alongside its own proprietary funds, marking the first time a major Wall Street broker has sold no-loads. Smith Barney could see a big drop in both revenues and assets under management if too many customers buy no-load funds, which carry a 1.5% annual "wrap" fee instead of the 5% up-front sales loads charged by Smith Barney's

in-house funds. "We're not a proprietary fund company," she says. "We're a full company period."

To keep Smith Barney's funds competitive against no-loads, Bibliowicz gearing up to exploit one of Smith Barney's biggest untapped assets: a network of 37,000 insurance agents and brokers in the Travelers organization licensed to sell mutual funds. That's more than industry leader Merrill Lynch & Co.'s 13,800 brokers. Bibliowicz also created a new group of asset-allocation funds, called the Concert Series, that will become a core offering in the company's 401(k) retirement program.

AXED. Perhaps more important, she has improved the performance of Smith Barney's in-house funds. Three years ago the firm had only two Morningstar-rated five-star funds. Now, there are seven. Paul Rice, a Morningstar Inc. analyst, says Smith Barney's 70 funds have a

JESSICA M. BIBLIOWICZ

EMPLOYMENT

1994-present, Executive vice-president, Smith Barney Mutual Funds

1991-1994, Director of sales and marketing, Prudential Mutual Funds

1982-1991, First V-P, Lehman Brothers, Shearson Lehman Brothers

1981-1982, Assistant manager, Gold Card Retention, American Express

EDUCATION

Cornell University, B.A. 1981

PERSONAL

36, Married, two children

EXTRACURRICULAR

Board member of the Investment Company Institute and council member of New York Hospital Medical Center

vanced from being below average in 1993 to "about average" through June. Among the funds that Bibliowicz axed was one run by market prognosticator Elaine M. Garzarelli (page 75), who "made good top-down calls, but didn't back them up with good stock picks," Bibliowicz says.

Bibliowicz has now become one of the highest-ranking women in the mutual-fund industry, along with Fidelity Investments' Abigail Johnson, daughter of Chairman Edward C. "Ned" Johnson III. And at just 36, she seems to be injecting into Smith Barney some decidedly newfangled thinking.

By Geoffrey Smith in New York

WHAT MADE ELAINE HOUT 'SELL'

Her model turned down days after she forecast a 6400 Dow

An old Wall Street adage says that you're only as good as your last market call. Nobody knows that better than Elaine M. Garzarelli, who as a senior partner at Lehman Brothers investment strategist turned bearish a month before the 1987 crash. That endeared her to the firm's brokers and clients and made her the best-known and perhaps best-paid woman on the Street.

So when Garzarelli, who now has her own firm, Garzarelli Capital Inc., told clients to get out of the market on July 23, traders paid heed. The Dow Jones industrial average had been up more than 40 points but had lost half of its gains by 12:45 p.m. when Bloomberg Business News flashed a one-line notice of a bearish turn. By 4 p.m., the Dow was down 44, with news reports giving Garzarelli a good part of the credit, depending on your view, the blame for the day's downturn.

In the week since, she's been getting neither credit nor blame but derision. The market has rebounded—"a good selling opportunity," she says. And the media and analysts pointed out that her bearish call came only a few days after she predicted in the *New York Times* that the Dow was heading for 6400.

IOUS SEER? Garzarelli says she "was as surprised as anyone" when, in a data revision, 14 indicators registered a 23.5% positive, well below the 30% sell trigger. Her market model (table) of monetary, economic, valuation, and sentiment indicators, had held around 80% positive for most of 1996 but had begun to deteriorate recently. In her July report, the indicators were only 48.5% positive. Still, Garzarelli remained bullish. Now, she says the market will drop 15% to 25% from the peak, which could take the Dow down to 4300.

Should you take this seer seriously? Garzarelli was right about the money for the 1990s bull market, having turned



BEAR: Now, she sees a 15% to 25% drop

bullish in the fall of 1990. The post-1987 showing, however, was mixed. She says her indicators turned bullish in early 1988, which was published in her reports. But she waited too long to buy

stocks for a mutual fund she was running. The fund never regained its edge and was shuttered in 1994.

Garzarelli's bear turn, like that of other market analysts, began in July. But not because of the day-to-day swings of the Dow. First, the coincident-to-lagging indicator ratio, a measure of economic strength, turned south. But that in itself was not fatal, since it has a small weighting in her overall system. More troublesome were rising interest rates for three-month Treasury bills. When the bill rate rises above the discount rate, it's bad news for stocks. "That tells you the Fed has room to tighten," she says. That indicator, which counts 10% in her model, further weakened the bullish case.

The indicator that broke the bull's back was corporate cash flow. That turned down on July 22, when Garzarelli's assistant, Alida Melkonian, received revisions on first-quarter corporate cash flow. Melkonian faxed them to Garzarelli at her home in the East Hampton, N.Y., woods. Cash flow plunged from the fourth quarter, as depreciation fell off 4% and deferred taxes sank 70%. The newly lowered cash flow yield could not stand up to higher interest rates, and that indicator turned negative. So she scheduled a conference call with her institutional clients for 11:30 a.m. the next day. These clients pay thousands a year for such calls, consultations, and reports.

Garzarelli planned to notify the 55,000 subscribers to the \$149-a-year *The Garzarelli Outlook* by hot line and fax, but word had already gotten out, as a money manager—one of about 60 in on the conference call—told Bloomberg. An hour later, CNBC reported the item as well. The leak, she admits, probably angered many subscribers, though her publisher says 35,000 on her "alert" service had been reached by 6 p.m. "Next time, I'll make my calls after the market closes," she says.

Garzarelli's fans needn't expect a bullish call soon. That's because some indicators depend on data that changes only monthly or quarterly. So, she says, it will be at least three months before the model can turn bullish. Of course, if the market turns decisively northward in the meantime, there'll be fewer people waiting for that call.

By Jeffrey M. Laderman in New York

Garzarelli's Key Indicators

	STATUS	WEIGHTING
VALUATION		
CASH FLOW YIELD VS. INTEREST RATES	Negative	20%
PRICE-EARNINGS RATIO	Negative	8
MONETARY		
THREE-MONTH T-BILL RATE	Positive	10
T-BILL VS. DISCOUNT RATE	Negative	10
INTEREST-RATE MOMENTUM	Negative	2
FREE RESERVES IN BANKING SYSTEM	Positive	1
SHAPE OF YIELD CURVE	Positive	1
MONEY SUPPLY GROWTH	Negative	1
RATIO MONETARY/ECONOMIC GROWTH	Negative	1
SENTIMENT		
MUTUAL FUND CASH LEVEL	Neutral -	12.5
NO. OF BULLISH ADVISERS	Neutral +	12.5
ECONOMIC		
EARNINGS GROWTH MOMENTUM	Negative	10
INDUSTRIAL PRODUCTION MOMENTUM	Negative	10
COINCIDENT/LAGGING INDICATOR RATIO	Negative	1

DATA: GARZARELLI CAPITAL INC., BUSINESS WEEK

COMMENTARY

By Nanette Byrnes

BUYBACKS MAKE NEWS, BUT DO THEY MAKE SENSE?

It's Olympics season, and everywhere you turn are images of track stars sprinting, jumping, and hurling their way to the gold. Sneaker maker Reebok International Ltd. is clothing some 3,000 of the athletes in Atlanta. But back at company headquarters in Stoughton, Mass., leaden sales growth has weighed heavily on the company's performance, as rival Nike Inc. has sprinted ahead with record earnings and sales. As a result, Reebok's stock was trailing. It was selling at 31—too low, management believed. So on July 29, the company announced its plan to buy 33% of its shares outstanding. Investors gave the move a standing ovation, bumping the stock up 10% in one day, to 34%.

Reebok's is just one of a record 842 repurchase announcements made so far this year, according to Securities Data Co. That's up from 655 in the same period last year, and 536 in 1994. If all 842 vows are kept, over the next few years \$93 billion worth of stock will be removed from public pockets and either retired or deposited in treasury or employee accounts at Walt Disney, IBM, Wells Fargo, and a host of other corporations. Purchases are getting bigger, too: In 1996, there have already been 20 announcements for \$1 billion or more, compared with 17 in all of 1995.

CASH FOUNTAIN. The reasons for buybacks vary. Many companies claim that their stock is undervalued and a good buy. By reducing the number of outstanding shares, per-share earnings will increase and boost the stock price. Philip Morris Cos. instituted a \$6 billion three-year buyback in 1994 not only to boost the stock but to absorb the company's fountain of free cash. BankAmerica Corp., which raised its repurchase to \$2 billion in March, lacked high-return investment options. "We look very hard internally," says Michael E. O'Neill, BofA's chief financial officer, "but if we don't have a use for capital we ought to return it to shareholders." Many companies are buying in stock for a tech-

nical reason: They need it in their treasuries so that insiders can exercise options.

But there can be downsides to buybacks—both for companies and investors. In the near term, they often do little to help the stock. Laszlo Birinyi of Birinyi Associates Inc.

a buyback. But beyond that, says David J. Denis, professor of finance at Purdue University's Krannert School of Management, "It's hard to get confirmed results." Buybacks, he adds, are "not a cure-all for everyone."

Using buybacks to sop up loose cash isn't always a good strategy, argues Samuel L. Hayes III, a professor at Harvard business school. He says that rather than jumping into stocks after a buyback announcement, investors ought to be asking why the company isn't investing in new product lines or boosting spending on marketing.

LITTLE HELP. Bob Gabele, president of CDA/Investnet, a firm which tracks insider stock ownership, questions the motivation of some corporate executives. He says many buybacks coincide with significant insider selling, which suggests that management may not really believe that its stock is undervalued.

Buybacks may not be much help to poorly performing companies. In his repurchase announcement, Reebok Chief Executive Paul Fireman attributed the buyback to "confidence in Reebok's prospects." But Faye Landes, footwear analyst at Smith Barney Inc., says the buyback does not address the company's fundamental market-share problems. "A buyback can't mask poor results," she says. Indeed, Reebok's buyback may even hurt the company. Unlike Philip Morris and General Electric, which buy stock with cash, Reebok is borrowing the money to buy in its shares, a bill that could run as high as \$864 million, quadrupling debt. Two rating agencies have moved to put the company's debt rating under review.

The lesson? Buybacks may help healthy companies. But if your company is lagging, look elsewhere for miracles.

Byrnes follows the markets from Los Angeles.



A \$6.4 billion buyback announced at Disney hasn't kept the stock from sinking 11%

points out that many of this year's big announcements have quickly fizzled. A \$6.4 billion buyback announced by Walt Disney Co. in April hasn't protected that stock from sinking 11% since, as entertainment stocks fell out of favor. "One should not buy stock based on a share buyback," Birinyi concludes. Only 75% of stock earmarked for buyback actually gets bought in anyway, he says.

Over the long term, academic studies show that a company's stock tends to rise for a year or two after

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BY GENE G. MARCIAL

BARGAIN HUNTING IN A SOFT MARKET

The stock market "will be a struggle" in the second half of 1996, Bill Priest says. The CEO and co-head of equity investing at BEA Associates, which manages \$28 billion in assets, expects the market will soften: Earnings may not be as good as in the first six months, and the Fed may nudge up interest rates. So Priest has been scouting for companies that are underpriced relative to their cash flow and intrinsic value.

Priest doesn't restrict himself to blue chip issues. Two picks he has bought recently are by no means

Street favorites: GTECH Holdings (GTK), the world's top supplier of computerized lottery products and services, and McKesson (MCK), a distributor of drugs, bottled water, and health and beauty aids. Both stocks have yet to sizzle. But Priest expects they will do so before long.

GTECH, at 26 a share—not far off its 52-week low of 23—is an attractive buy-out candidate, notes Priest. The company runs online systems for 28 lottery authorities in the U.S. and in 49 foreign markets. It has an 80% share of government-run lottery contracts worldwide. "I am not privy to any inside stuff," says Priest. "But I think GTECH would be a good fit with financial companies such as GE Capital, NationsBank, or Citicorp." As Priest sees it, GTECH needs to link up with a big financial name because of the regulatory hurdles it has to clear in every state or country in which it operates. In particular, Priest says, NationsBank's Hugh McColl is the "imaginative and innovative kind of CEO" who would see the advantage of what GTECH can offer. Priest thinks GTECH is cheap and will eventually be worth 40 to 45 a share. BEA Associates owns about 1 million shares, or 2.3% of the stock outstanding. "One big smart investor in GTECH," says Priest, is Tiger Management, with 15%.



PRIEST: GTECH and McKesson

McKesson is another gem, says Priest. CEO Alan Seelenfreund and new President Mark Pulido are "very shareholder-oriented," says Priest. He thinks Pulido will raise profit margins in McKesson's core businesses and then divest noncore operations, such as its 55% stake in Armor All Products, a marketer of car-care goods. McKesson has sold off assets and holds about \$475 million in cash and marketable securities. Priest thinks Pulido will continue buying back shares. Priest figures McKesson, now at 43, is worth 65 to 70.

TWO WAYS TO GET PUMPED UP

No matter how it ends, the quest for Commercial Intertech (TEC) may yield a win-win situation for some risk players. Interotech is trying to thwart a June 27 hostile takeover bid from United Dominion Industries, which on July 25 increased its offer from 27 to 30 a share.

Interotech, a maker of hydraulic components, building products, and fluid-purification systems, escalated the fight on

July 29 by announcing the spin-off of its profitable Cuno unit to stockholders. Each shareholder will receive one newly minted Cuno share for each share of Interotech held as of Aug. 9. Cuno will soon apply to trade on Nasdaq. Interotech's stock rose to 29% after Dominion made its initial offer—then slumped to 26 when the bid was rejected.

Analysts expect Dominion to mount a legal challenge to the proposed spin-off. Even so, some pros argue that Interotech is still a good buy. Why? Interotech's Cuno, which also makes fluid-purification systems, is worth \$200 million, or 14% a share based on 13.7 million shares, according to one investment banker. He feels that Cuno's worth could double in a year or so, whether or not the spin-off happens. Dominion may opt to raise its offer for Interotech, especially if its real target is the Cuno operations, says this pro.

FEELING A HYDRAULIC LIFT



COMING UP TRUMPS IN THE SLUMP

This money manager went shopping for stocks—in the depths of the market's mid-July slide—and came out a winner. From July 16 through July 24—when the market was badly battered—the portfolio of Catherine Lawson, chairman and chief investment officer of Highland Investment Group gained 0.10%, vs. a loss of 0.32% for the Standard & Poor's 500-stock index. Highland also did well in the longer term: From Sept. 30, 1995, through July 24, 1996, its stocks gained 6.4% compared with the S&P's 0.47%.

Lawson is high mainly on small-caps. One of her latest favorites is PETSMART (PETM), which operates nearly 300 pet superstores, specializing in food, supplies, and services. Another is Express Scripts (ESRX), a provider of pharmacy-management services—including mail-order medicine—designed to contain costs of prescription drugs.

PETSMART has been on a quite a roll this year: Its stock has nearly doubled, from 12% a share in mid-January to 22% by July 30. Lawson figures it will hit 30 before yearend. She expects PETSMART's expansion will continue, adding about 60 stores this year. She also looks for profit growth: 85¢ a share in the year ending Jan. 30, 1997, and \$1.22 in fiscal 1998. "Demand for these one-stop pet superstores is growing by leaps and bounds," says Lawson, who notes that PETSMART's slice of the \$32 billion pet business is still only 4%. She sees it doubling in a couple of years.

Express Scripts, trading at 35, is down from 58 in mid-January. But Lawson sees it snapping back to the upper 50s. The business is capital-intensive, notes Lawson, but there's substantial growth ahead. And with its stock way down, Express Scripts is "bound to be taken over," says Lawson. It is, she adds, "the last remaining independent mail-order drug stock."



LAWSON: High on small-cap stocks

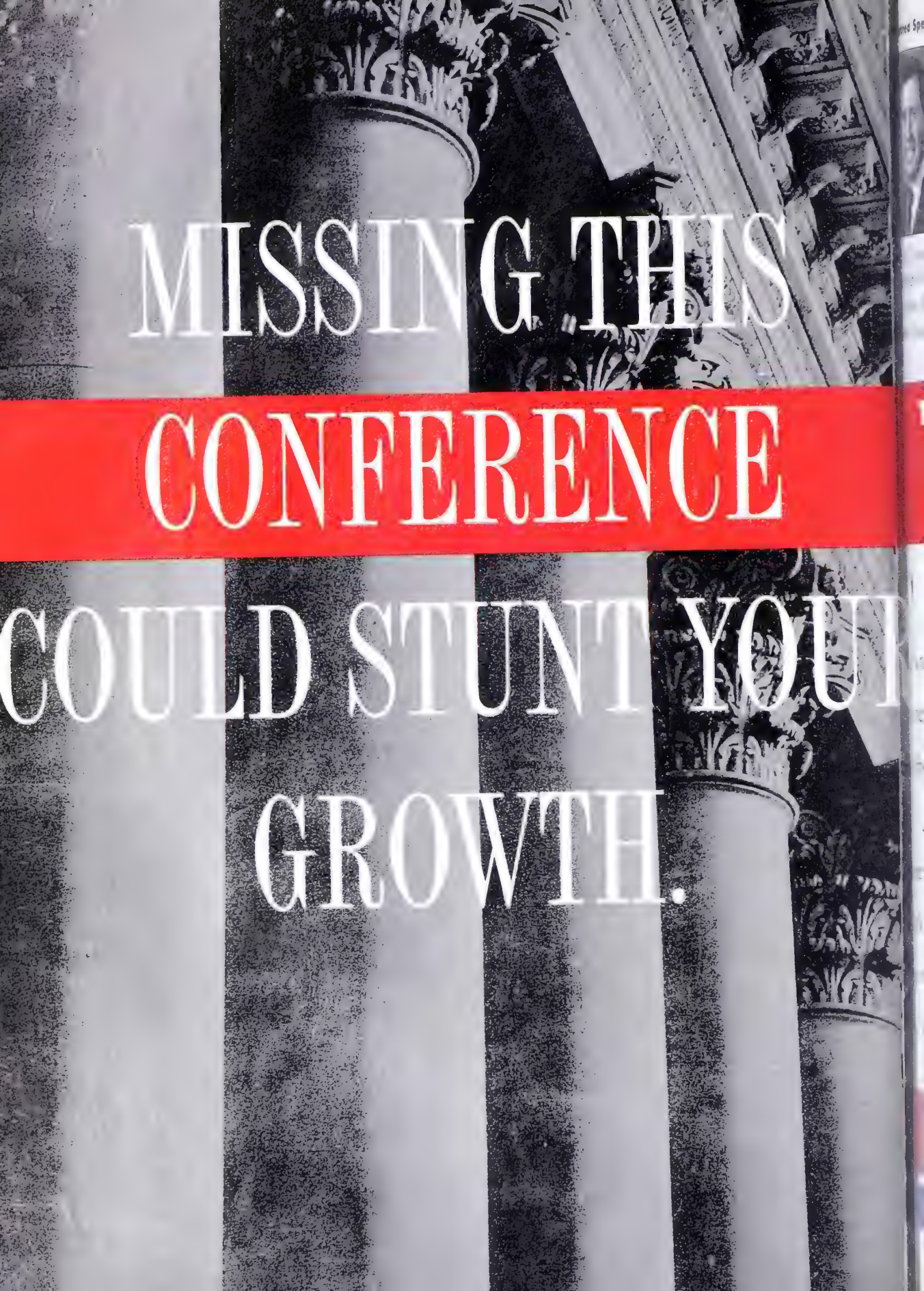
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INTERNATIONAL  PAPER

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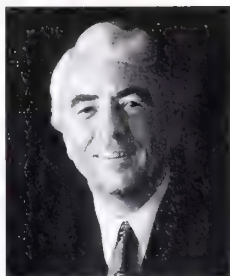
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EDITED BY PETER COY

THE ULTIMATE INDEXING JOB

THE INTERNET WILL PUT MORE DATA ON p than any other technology in history. That's the promise—and the problem. As anyone who has used a search tool such asahoo! or Alta Vista knows, weeding out the irrelevant "hits" can try one's patience. And it's getting worse. If businesspeople can't find critical information quickly, the Net's potential could be crippled. To avoid that, researchers at the National Center for Supercomputing Applications (NCSA) in Champaign, Ill., are developing an indexing scheme similar to the one used by librarians. It's part of the federal government's Digital Library Initiative—and it's turning into a far bigger job than expected.

The NCSA team, headed by researcher Bruce Schatz, tested the approach with 10 million abstracts from the engineering library at the University of Illinois at Urbana-Champaign. They decided to have computers segregate them into 1,000 subject areas after analyzing their content. But creating indexes for even this comparatively small sample quickly overwhelmed the team's workstation computers. So the job was transferred to one of NCSA's supercomputers, which cranked away for four days. Schatz says indexing may well turn out to be the toughest problem NCSA has ever undertaken.

Otis Port

INDIA CALLS IT PATENT SURDITY

A CASE THAT PITS EAST against West, India's Council Scientific & Industrial Research is fighting a patent awarded to the University of Mississippi Medical Center for medicinal use of turmeric, the old Indian spice.

The Indian organization is asking the U.S. Patent Trademark Office to revoke the 1993 patent on grounds that the medicinal properties of turmeric have been known in India for centuries. But the two Indian-born physicians at the Jackson (Miss.) medical center, who obtained the U.S.

patent, immunologist Harihar Cohly and plastic surgeon Suman K. Das, say they brought scientific credibility to the traditional remedy, which is ap-

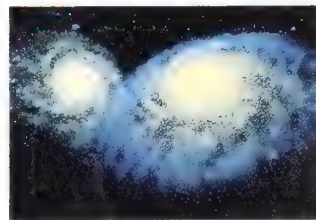


plied to open wounds. They also say they won't seek a patent in India.

The case recalls a similar debate over India's neem tree, whose seeds contain a natural pesticide. Nongovernmental groups in India are fighting some 26 international patents that have been issued for industrial processes related to the neem tree. They regard the patents as corporate theft from the Indian people.

Western companies say they need patents to justify investments in products based on traditional remedies. In a current case, patent concerns have kept some drug companies from developing products based on artemether, a Chinese herbal medicine that fights a form of malaria resistant to quinine. □

INNOVATIONS



■ In 1964, IBM produced a science movie for school kids called *Powers of Ten* that led viewers from the hand of a sunbather outward to intergalactic space, and then inward to an atom's nucleus. A high-tech remake called *Cosmic Voyage* premieres on Aug. 9 at the Smithsonian Institution's National Air & Space Museum in Washington. The 35-minute film, in the IMAX format, was sponsored by the Motorola Foundation with support from the National Science Foundation. Its interstellar simulations, which includes a collision of two galaxies (photo), required 950 hours on a Cray C90 supercomputer.

■ What hazards await on foreign shores? At a Web site created by SafeReturn, a unit of Multimedia Medical Systems in Reston, Va., you can browse a geographic database outlining biological, environmental, and political risks. The terse "alerts" at the site (<http://www.mdtv.com/safe.html>) are updated daily to reflect coups d'etat, toxic-waste spills, or cholera outbreaks.

TIME TO HARVEST? LET THE ROBOT DO IT

FIRST COUSIN OF DANTE, the volcano-exploring robot, is heading for the wide alfalfa fields of El Centro, Calif., this month. The mission of this agricultural robot, known as Demeter: to put harvesting machines on automatic pilot.

Demeter, developed for

New Holland North America Inc. at the NASA Robotics Engineering Consortium at Carnegie Mellon University, uses artificial vision to follow rows, while checking its location with the help of global-positioning satellites. It's designed to hum along, driverless, at 10 mph, com-

pared with 4 mph for harvesters run by skilled farmers. And it should go as quickly at night as in daylight.

The first marketable product, which is scheduled to come out next year, will be a \$5,000 retrofit that improves the yields of existing harvesters. Using cameras to guide the machine and

software to adjust the height of the cut, this system would still call for a driver on board in case it goes haywire.

But New Holland hopes to market a commercial version of a thoroughly modern Demeter in a couple of years. The timing might depend on how the robot fares this summer. *Stephen Baker*

SECURITY

AN END TO ANONYMOUS BOMBS?

Even the NRA may not be able to stop IDs for explosives

Tagging explosives with minute chemical markers to help the FBI track down terrorists ought to have surefire voter appeal. In the aftermath of the fiery crash of TWA Flight 800 and the bombing in Atlanta's Centennial Olympic Park, a proposal to require such "taggants" is once again at the center of Washington debate.

Requiring explosives makers to mix in the telltale markers might seem innocuous enough, but over the past 20 years such proposals have been regularly carted up to Capitol Hill and just as regularly rejected—most recently last year, when Congress shot down such a proposal. Instead, it authorized a study of their effectiveness—and then refused to fund it. Legislators retreated in the face of vehement opposition from the National Rifle Assn. and explosives makers, who claim that taggants are costly and potentially deadly.

RAINBOW CODE. It's all a smoke screen, retorts Charles W. Faulkner, general counsel at Microtrace Inc. in Blaine, Minn., the oldest supplier of tags. "All these rumors have been floating around for years," he says. "What they conveniently ignore is that we've been supplying Microtags to Switzerland for 13 years, with no safety problems." Switzerland mandates the tagging of all explosives made within its borders.

Faulkner admits opponents are right when they project costs of hundreds of millions of dollars for explosives makers. But he prefers to put the costs in a different light. On a per-pound basis, he says, taggants "would be 2¢ or less."

The tags that Microtrace sells were



OKLAHOMA CITY: New taggants can identify homemade bombs

invented in the early 1970s by Richard G. Livesay, a chemist at 3M. They are tiny plastic chips no bigger than a grain of pepper. The chips have 10 layers, each a different color, that can be stacked in

millions of combinations. So a distinctive rainbow code can identify each manufacturer, batch of explosives, and its distributor.

From 1977 to 1979, a federal

test of 3M's technology put taggants on 1% of all explosives made. When a truck blew up in Baltimore in May, 1979, killing Robert J. Riffe, tags found in the wreckage quickly led federal agents to James L. McFillin. He was convicted that December. In Switzerland, the tags have helped solve 566 bombings over a decade, according to the Office of Technology Assessment (OTA).

However, things started to go sour for 3M in July, 1979. A blast at the General Explosives plant in Camden, Pa., Ark., was blamed on the taggants. General

sued. 3M was exonerated, but opponents of tagging still cite the incident as a danger signal. The following year, Congress called a halt to the test under pressure from critics. 3M later sold the technology to Livesay, who founded Microtrace. Today, says Faulkner, the tags are used mainly as anticounterfeiting markers for consumer goods, including shampoo and alcohol, as well as for placement pasters for planes and trucks.

Now, a new tagging technology is being marketed by Isotag LLC in Houston. And it could undermine a crucial point of

opposition: that no practical method exists for tagging ammonium nitrate, which was used in the bomb that devastated the federal building in Oklahoma City in 1995.

Isotag's chemical markers are very rare, heavyweight molecules that can be detected in extremely low concentrations—one taggant molecule among millions of product molecules. They are now used mainly to identify natural gas and petroleum products flowing through pipelines.

In 1993, a fertilizer company wondered if Isotag's markers could survive an ammonium nitrate explosion. Tests showed

TWO LEADING TAGGANT MAKERS

MICROTRACE Ten-layer structure of tiny "paint chip" provides millions of color combinations. Tags can pinpoint manufacturer, distributor, and even date of production.

ISOTAG Taggant molecules are made by replacing hydrogen atoms with their heavier cousins, deuterium. This and other modifications can provide millions of chemical tags.

y could. "Tagging with the old technology costs \$65 to \$100 per ton" of id, says Isotag President D. King Anson. But with Isotag's markers, he res the cost would be about \$7 a ton. Perhaps the most effective opposition taggants has come from the NRA, ch argues that their use in gunpow- would raise serious safety issues for 3 million members. For example, if ratio of tags to gunpowder varies, would the explosive punch of bullets. me rounds might be so powerful they ld blow up in the gun," says NRA kesman Chip Walker. The organiza- is not opposed to tagging high ex- sives, like dynamite and plastic, or cultural chemicals, such as ammonium ate.

MINO EFFECT? However, the U.S. anies that produce 4 billion pounds explosives have their own worries. Institute of Makers of Explosives e), a Washington lobbying group, fig- s that tags would increase costs by 0 million a year in the mining industry e. As for safety, the IME points to a 0 study by the OTA that found signs t taggants reduce the stability of ex- sives. Jimmie Oxley, a professor of mistry at the University of Rhode und, recently analyzed some tagged and says she was "surprised to find that it changed the thermal proper- of the TNT." This change could make more dangerous to work with.

The availability of a practical way to ammonium nitrate, combined with political demands for new antiterror- legislation, could mean that explo- es tagging now has a chance of be- ing law. Walker says the NRA would ept tagging if an independent, scien- e study determined it is safe.

If tagging were required in the U.S., ne 90-odd other countries might shift rs and speedily follow suit, tightening worldwide supply of bomb-grade ex- sives. At a meeting of the Interna- al Civil Aviation Organization in 1991, years after the bombing of Pan Am ght 103 over Lockerbie, Scotland, half the ICAO members signed a treaty "in nciple" to require the tagging of ex- sives. But five years later, only 22 ntries have ratified the treaty. For it take effect, 35 are required.

Representative Charles E. Schumer (N.Y.) believes that tagging now nds a real chance. "But unless Con- ess stands up to the NRA, it is going to extremely difficult to get this impor- it legislation done," he says. The U.S. s been playing with tagging long ough. Congress may finally be ready to e a stand.

By Otis Port in New York, with therine Yang and John Carey in ashington

Information Processing

PERIPHERALS

ZIP DRIVES NEED A BIT MORE ZIP

To keep growing, Iomega must make them a PC standard



The ads for Iomega Corp.'s Zip disk drives are certainly catchy. They show people in a variety of scenes, getting big news from an obstetrician or a probate lawyer, who interrupt to ask the improbable question: "Is that a Zip drive on your desk?" The gag—that a superhigh-capacity floppy disk could be absolutely fascinating—has worked. The Zip is one of the hottest-selling PC accessories around.

Now, however, Iomega must do something more: It needs to make the Zip fascinating enough for computer makers to build into their machines—or the highflying company could be in for a slowdown. The Roy (Utah) company, which has been building data-storage products for 15 years, finally took off two years ago after overhauling its disk- and tape-drive lines—and pitching them directly to consumers. Iomega became one of the fastest rising stocks on the NASDAQ, thanks in part to computer enthusiasts who hyped it in online discussion groups. The shares rose a hundredfold, from a split-adjusted 0.54 in the first quarter of 1995, to a peak of 55 in May.

EDWARDS: "The third quarter will be challenging"

But by the end of July, the stock had fallen to 15%. Second-quarter sales and profits met or ex-

ceeded analysts' expectations, but investors were spooked by signs of increased competition and slowing growth: Iomega's second-quarter order backlog was down, and its inventory of finished goods was up, due partly to slow sales in Europe. Things may not turn around quickly, either. "The third quarter will be challenging," concedes Chief Executive Kim B. Edwards.

MARKETING BUZZ. Has Iomega hit a wall? Not yet. Analysts haven't slashed their bullish 1996 projections. J.P. Morgan & Co. analyst Daniel Kunstler predicts revenue of \$1.3 billion and earnings of \$67 million, more than eight times last year's figure (chart, page 86). But now there are questions of just how far Iomega can go. If the company can make the Zip drive the successor to the standard 3½-inch, 1.44-megabyte floppy drive found on all PCs, it could see its volumes swell from an estimated 5 million units this year to nearly 40 million

Information Processing

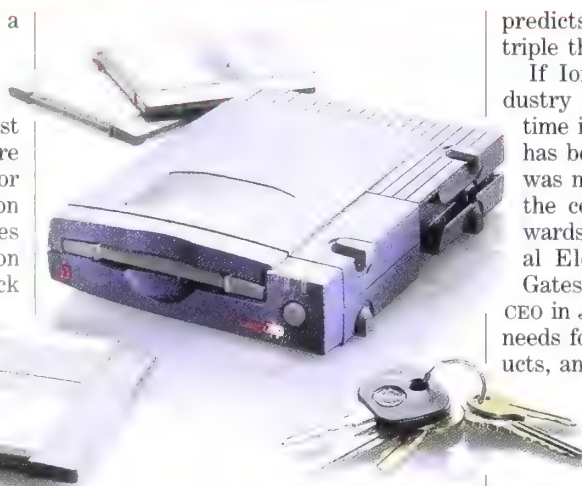
in 2000. If not, Iomega could remain a niche supplier of specialty drives.

The only way to make the Zip a standard is to go beyond selling it as an aftermarket accessory. In the past 18 months, the company has sold more than 2 million drives, which retail for about \$200 and hold 100 MB of data on pocket-size, removable disk cartridges that cost about \$20. The Zip caught on because it was a simple way to back up information stored on a computer hard disk or to transfer massive files—and because Iomega created a marketing buzz around removable backup storage, historically a sleepy product category.

Iomega's challenge now is to persuade PC makers to design the drives into every one of their machines. But the Zip isn't the only option. PC giant Compaq Computer already has chosen a Zip alternative, the LS-120 drive, backed by 3M and Matsushita-Kotobuki Electronics. It costs about the same as the Zip but has one huge advantage: It is "backward-compatible" with conventional 3½-inch floppies, which means it can read and write information on such disks—an estimated 5 billion of which are now in use. With the LS-120, computer makers could use a single drive to replace the floppy. But with Iomega, they would need to have the Zip and a conventional floppy drive, too.

CHICKEN OR EGG. There are other Zip alternatives, as well. One is a 128-MB, backwardly compatible drive under development by floppy-disk giant Mitsumi. Further out, meanwhile, are recordable versions of the Digital Video Disk (DVD), the 6-billion-byte replacement for the CD-ROM.

For Iomega, it all boils down to a classic chicken-or-egg situation. Some PC makers remain unconvinced that there's huge demand for Zips. Packard Bell Electronics Inc. offers them as options in a few models, but "consumers are not clamoring for a Zip drive in their PCs," says Packard Bell Marketing Vice President Mal Ransom. Dell Computer Corp. can't offer the Zip as an option because corporate customers are



PC makers are offering Zip drives, but so far their commitment is limited

leery of providing employees with an easy means of walking off with huge data files, according to marketing manager Neil Hand.

PC makers also are reluctant to pay the price to build in Zip drives. The standard floppy drives they now use cost them about \$20. Iomega charges computer companies \$70 to \$80, analysts estimate.

So far, that has limited the Zip's acceptance by PC makers. Only a handful of them offer it, and only on a few high-end models or as an option. IBM, Acer, Hewlett-Packard, NEC, Packard Bell, Micron, and three other companies have signed up. "They're only testing the waters," says analyst Todd D. Bakar of Hambrecht & Quist.

Edwards acknowledges that sales through PC makers were "insignificant" in the second quarter. But Hewlett-Packard Co. and NEC Corp. recently announced plans to expand use of the Zip in additional models. Analyst Cliff Josephy of brokerage H. D. Brous & Co.

predicts that sales to PC makers will triple this quarter.

If Iomega can make the Zip an industry standard, it will be the second time in three years that the company has beaten the odds. In 1993, Iomega was moribund—sales had stalled, and the company was losing money. Afterwards, a marketing veteran of General Electric Co. and battery maker Gates Energy Products who became CEO in January, 1994, recognized critical needs for customer research, new products, and aggressive marketing.

That's how the Zip was born. But when Iomega approached PC makers about buying the drives, they were skeptical that customers would pay for the higher-capacity floppy. Iomega took the product directly to consumers. "We had to prove that there was huge acceptance in the aftermarket before we could get PC makers excited," says Iomega Marketing Vice-President Timothy L. Hill. By mid-1995, Zip drives had caught on. Revenues jumped from \$141 million in 1994 to \$326 million in 1995—mostly from Zip sales. For the first six months of 1996, sales hit \$500 million, up a staggering 445% from the first half of 1995.

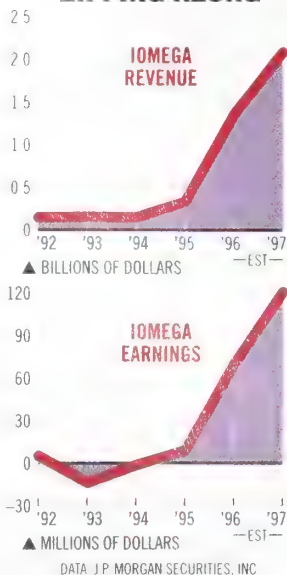
A BILLION BYTES. Before Iomega gets PC makers to commit to buying large quantities of drives, though, it not only must prove there will be sufficient demand, it must also push down prices and assure PC makers that there's a reliable supply from multiple sources. On the pricing front, Iomega has started to offer a \$50 rebate to consumers, part of a planned price-cutting strategy, Edwards says. The company's goal is to bring the price down to \$99 at retail and less than \$50 for PC makers.

On the manufacturing front, both Iomega and the LS-120 camp are scrambling to add capacity. Matsushita announced that Mitsubishi Electric Co. would build the LS-120 starting in early 1997. Most Zip drives are now made under contract by Seiko Epson Corp. Iomega recently purchased a factory in Penang, Malaysia, where it will build its new \$500 Jaz drive, which features a 1-billion-byte removable disk cartridge costing \$150, in the fourth quarter. The factory may produce Zip drives next year, as well.

With the new plant, Iomega will be able to match its competitors' output. Now, all it has to do is make sure that storage enthusiasts aren't the only ones lining up to buy the new drives.

By Andy Reinhardt
in San Mateo, Calif.

ZIPPING ALONG



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A SURPRISE PARTY FOR CORPORATE AMERICA

Free-spending consumers fueled an 11% leap in second-quarter profits

What's going on? Just as everyone got used to the idea of declining profit growth, Corporate America uncorked another surprise. Thanks to a consumer-fueled economy that beat expectations, earnings for the 900 companies on BUSINESS WEEK's Corporate Scoreboard rose 11%, to \$81 billion, on a sales increase of 8%, to \$1.2 trillion. Following two disappointing quarters, the news left many

scratching their heads. "Profits numbers have a habit of surprising us to the upside," says John Ryding, senior economist at Bear, Stearns & Co.

The biggest positive jolt came from U.S. consumers, who kept on spending even though their levels of indebtedness continue to rise. That's because accelerating employment numbers and a strong stock market—at least until recently—boosted consumer confidence.

The economy was also lifted by increased capital spending, steady export and industrial production growth. The uptick in spending came just as many companies had pared inventories. Now with demand healthy, they're beginning to build them up again. "The slowdown has not materialized," says Donald Straszheim, chief economist at Merrill Lynch & Co., "and that is translating into profits."

Winners and Losers in Quarterly Earnings

THE INDUSTRIES

THE COMPANIES

THE LEADERS

PERCENTAGE CHANGE FROM 1995'S SECOND QUARTER

AEROSPACE & DEFENSE	416%
GENERAL MANUFACTURING	184
APPLIANCES	143
STEEL	83
APPAREL	66
RAILROADS	54
FINANCIAL SERVICES	49
COAL, OIL & GAS	47
BUSINESS MACHINES & SVCS.	39
TEXTILES	38
AIRLINES	38
GLASS CONTAINERS	37
PETROLEUM SERVICES	35
HOTEL & MOTEL	34
CARS & TRUCKS	31

THE LAGGARDS

PERCENTAGE CHANGE FROM 1995'S SECOND QUARTER

FOREST PRODUCTS	-85%
BUILDING MATERIALS	-71
PAPER CONTAINERS	-70
CONSTRUCTION/REAL ESTATE	-59
FOOD PROCESSING	-53
PAPER	-37
NONFERROUS METALS	-33
FOOD DISTRIBUTION	-30
ALUMINUM	-28
COMPUTERS & PERIPHERALS	-25
SEMICONDUCTORS	-22
ELECTRONICS	-19
PUBLISHING & BROADCASTING	-16
FOOD RETAILING	-12
POLLUTION CONTROL	-11

WHO MADE THE MOST

MILLIONS OF DOLLARS

GENERAL MOTORS	\$2,096
GENERAL ELECTRIC	1,908
FORD MOTOR	1,903
PHILIP MORRIS	1,621
EXXON	1,570
AT&T	1,523
IBM	1,347
COCA-COLA	1,050
INTEL	1,041
CHRYSLER	1,037
DUPONT	1,001
MERCK	972
CITICORP	952
CHEVRON	872
CHASE MANHATTAN	856

WHO LOST THE MOST

MILLIONS OF DOLLARS

OWENS CORNING	-\$473
DIGITAL EQUIPMENT*	-433
ELECTRONIC DATA SYSTEMS	-327
NABISCO HOLDINGS	-216
CONAGRA*	-194
SMITH'S FOOD & DRUG CENTERS	-133
KAUFMAN & BROAD HOME	-98
DEAN FOODS*	-86
GENERAL INSTRUMENT	-58
NOVELL	-55
BRADLEES**	-54
GUIDANT	-46
CALDOR**	-43
KMART**	-38
FEDERATED DEPT. STORES**	-38



But will the economy keep turning pleasant surprises on the profit front? Most economists still think economic growth will slow in the second half of 1996—to 2.4%, according to *Blue Chip Economic Indicators*, a monthly survey based in Alexandria, Va., of leading business economists—especially if the Federal Reserve raises interest rates. Yet few expect a slump: “What we’re going to see is a slowdown in real growth, not a decline in profits,” says Ryding.

The second-quarter results were indeed impressive. General Motors Corp. topped the list of BUSINESS WEEK’s top second-quarter profit makers, even though its income grew by a paltry 1%, to \$2.1 billion, on a 6% revenue gain. Profits at GM’s North American auto operations grew by a more substantial 6%, however.

GM’s numbers actually trailed the industry’s: Carmakers overall saw second-quarter profits climb 31%, to \$5.1 billion, an 8% revenue gain. Chrysler Corp.’s earnings climbed a tremendous 668%, to \$1 billion, on a 27% sales increase, to \$3.6 billion. That’s because its new minivans are barreling out showroom doors. Rate reductions also helped profits.

SETTING. While the U.S. market for cars and trucks was surprisingly strong the first half of 1996, slower June sales have Wall Street fretting about the rest of the year. Analysts say the first three could face problems, particularly if the dollar strengthens against the yen. And some worry that higher interest rates and energy prices could hurt the consumer off. “While demand is running at relatively healthy levels, it’s unclear if this is sustainable,” says analyst Stephen J. Girsky of Morgan Stanley & Co.

Considering entire industries, America’s coal, oil, and gas companies posted the best gains, with collective profits of \$17 billion, an increase of 47% over 1995’s second quarter. Both oil prices and natural-gas prices rose, on strong

demand and a cold winter. One leader was Mobil Oil Corp., which saw its profits leap 337%, to \$783 million. In 1995, second-quarter results were hurt by a restructuring charge. Yet here, too, the gains were far from uniform. Weaker chemical prices meant that profits at Exxon Corp.—which gets more of its earnings from chemicals than Mobil—declined by 4%, to \$1.6 billion. “It made a difference what your product slate was,” says Holly R. Gustafson, an analyst at NatWest Securities Corp.

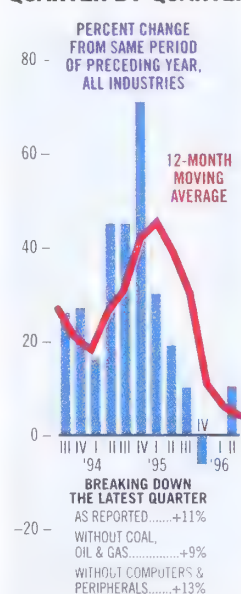
Cost-cutting continued to come to the aid of second-quarter profits in such consolidating sectors as aerospace and defense. The industry’s profits rose a stunning 416%, to \$1.4 billion, on a sales gain of just 10%, led by Boeing Co. Boeing’s earnings were \$468 million, a vast leap from its \$231 million loss in 1995’s second quarter—brought about

by restructuring charges. The world’s largest planemaker benefited from healthy orders. Not only is Boeing building more aircraft, but it’s also working to do so more efficiently. “[Boeing] is a cash monster,” says analyst Nicholas Heymann of NatWest Securities.

“SPECTACULAR.” Wall Street was another second-quarter profit center, thanks to still-heavy trading volumes and substantial investment-banking fees from the boom in mergers and acquisitions. Profits at financial-service firms jumped 49%, to \$5 billion. The largest relative gains came from Salomon Inc., which reported income of \$291 million, up from a loss of \$60 million. But with the market fluctuating wildly, Salomon’s—and the Street’s—gains may slow. “Salomon has put together a spectacular string of earnings,” says Michael Flanagan, a Philadelphia securities-in-

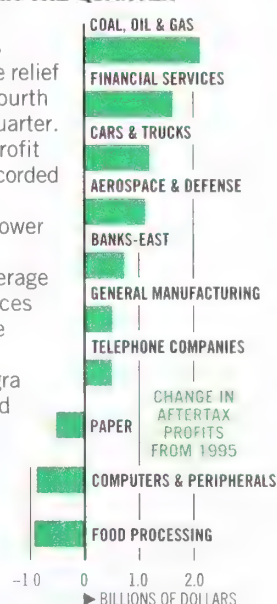
A Spotlight on Second-Quarter Profits

AFTERTAX PROFITS QUARTER BY QUARTER



INDUSTRIES WITH THE BIGGEST DOLLAR CHANGE IN THE QUARTER

What earnings slowdown? The second quarter’s 11% jump in profits is a welcome relief after the 6% drop in the fourth quarter and the flat first quarter. Another plus: The 6.6% profit margin is the highest yet recorded in a quarterly scoreboard. Higher oil prices helped power the oil companies (except for Exxon), while the brokerage firms made financial services a winner. There were some disappointments: food processing (hurt by ConAgra and Nabisco Holdings) and computer makers. Note, too, that sales growth has slowed to 8% this quarter from the 13% gain tallied in last year’s second quarter.



DATA: STANDARD & POOR’S COMPUSTAT

"The slowdown has not materialized, and that is translating into profits"

dustrial analyst. "But the odds are against them extending the streak."

Despite generally upbeat news, the second quarter had some losers. Rising commodity prices and tight pricing hurt food-processing companies. Overall earnings in the sector plummeted 53%, to \$825 million, including restructuring charges. ConAgra Inc., for example, lost \$194 million because of a \$508 million charge to close or reconfigure plants, shed about 7% of its workforce, and adopt new accounting rules.

Then, there was the computer hardware industry, which recorded an overall 25% earnings decline, to \$2.8 billion.



Digital Equipment Corp. posted a \$433 million loss, caused in part by a \$492 million restructuring charge, down from a \$160 million profit a year ago. Its woes stemmed from weak personal-computer and European sales. Not every such outfit was hurt: Compaq

Computer Corp. reported second-quarter earnings up 9%, partly because of better inventory and cash management. SBC CEO Eckhard Pfeiffer: "We all need to be able to deal with lower growth."

Cyclical industries such as paper were hurt by lower demand and gyrating prices. Since papermakers had hiked capacity in flush times, they were hit doubly hard. Industry earnings declined 37%, to \$911 million. Still, the second quarter story had a happy ending for most of Corporate America: The surprise profits party was still in full swing.

By Lori Bongiorno in New York, with bureau reports

THE LOUD LAMENT OVER A REBOUNDED BUCK

Last year was a picnic for U.S. exporters: The dollar's swoon improved American competitiveness, and profits boomed accordingly. Yet with the dollar up as much as 38% against the yen since April, 1995, it is no wonder many companies are nostalgic for days gone by. Multinationals such as Caterpillar Inc. and IBM are hoisting warning flags, citing the strong dollar as a potential profit pitfall.

They have a point: A strong dollar makes U.S. exports more expensive. With foreign sales rising as a percentage of total U.S. corporate sales, the impact is greater than ever before. And the comparison with 1995 is especially tough on multinational exporters. "Last year, you had this big wind at your back," says David W. Tice, president of David W. Tice & Associates, a Dallas investment adviser. "This year, you've got the wind in your face." Tice thinks the strong greenback will cause profits to drop in 1996's second half.

NOT "DRAMATIC." Yet the hand-wringing is only partly justified. Here's why: Although the dollar's rise against the yen hurts companies with mainly Japanese rivals, such as Caterpillar, the dollar has been nearly flat relative to the Canadian dollar, the currency of America's largest trading partner. Adjusted to reflect how much business the U.S. does with each of its trading partners, the value of the dollar has risen about

8% in the past 12 months (chart)—not insignificant but not shocking either. "I don't think the dollar is doing anything terribly dramatic," says L. Douglas Lee, chief economist at HSBC Washington Analysis, an economic research group. Even in Japan, Lee points out, economic recovery could well offset some of the yen-dollar rate changes by boosting demand.

What's more, the dollar has drifted downward a bit recently, thanks, in part, to the stock market declines and the Bundesbank's decision not to cut rates. As of July 29, a dollar bought 108 yen, down from its July 8 high of 111. While many economists think the dollar will rise if Alan Greenspan and the Federal Reserve Bank boost short-term interest rates on August 20, few expect it to soar beyond its June highs anytime soon. Martin Barnes, managing editor at Bank Credit Analyst, a Montreal economic-research publishing group, thinks the dollar is more likely to fall than rise, citing the upcoming U.S. Presidential election and the likelihood that the U.S. trade deficit won't improve much more.

Since the dollar's greatest weak-

ness came during April, 1995, the second-quarter numbers for 1996 should have showed the toughest comparison. "We felt the biggest impact in the second quarter," says David G. Shulman, chief equity strategist at Salomon Brothers Inc. "It's going to lessen as we get further into the year." Yet many of the companies citing exchange-rate concerns posted better-than-expected profit numbers, thanks to solid demand, both domestic and international: Their short-term margins actually improved.

Are multinationals just blowing smoke about the buck? Not exactly, says John Praveen, senior international economist at Merrill Lynch & Co. With corporate profit growth increasingly erratic and with wage pressures be-

ginning to pick up, the last thing anyone wants to worry about is a competitiveness problem with overseas rivals. Hence the corporate saber rattling. "It's a preventive-strike kind of thing," he says. "I don't think right now they're all that hurt." If the second quarter's profits are any indication, the pain so far is more imaginary than real.

By Jennifer Reingold in New York

STILL A LOW DOLLAR



Second Quarter 1996

CORPORATE SCOREBOARD

Glossary

SALES: Includes all sales and operating revenues. For banks, includes all operating revenues.

FITS: Net income before extraordinary items. For banks,

profits are net income after security gains or losses.

MARGINS: Net income from continuing operations before extraordinary items as percent of sales.

RETURN ON COMMON EQUITY: Ratio of net income available

for common stockholders (most recent 12 months) to latest available common equity, which includes common stock, capital surplus, and retained earnings.

PRICE-EARNINGS RATIO: Based on July 19, 1996, common-

stock price and corporate earnings from continuing operations before extraordinary items for most recent 12-month period.

EARNINGS PER SHARE: For most recent 12-month period. Includes all common-stock equivalents.

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE-EARNINGS RATIO 7-19	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1996 \$ MIL.	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL.	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL.	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL.	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
ALL-INDUSTRY COMPOSITE	122323.3	8	2410624.3	9	81059.3	11	153313.6	6	6.6	6.5	16.2	18	2.33
AEROSPACE & DEFENSE													
INDUSTRY COMPOSITE	26302.7	10	47303.4	2	1405.1	416	2310.3	135	5.3	1.1	11.8	24	3.08
BOEING	6275.0	13	10568.0	0	468.0	NM	587.0	NM	7.5	NM	10.2	29	3.00
GENERAL DYNAMICS	930.0	32	1823.0	25	67.0	10	132.0	9	7.2	8.7	16.1	15	4.08
LOCKHEED MARTIN	7076.0	26	12185.0	8	299.0	NM	571.0	580	4.2	NM	19.6	14	5.84
RAYDONNELL DOUGLAS	3261.0	-17	6423.0	-11	188.0	11	386.0	18	5.8	4.3	-11.9	NM	-1.57
ROTHROPP GRUMMAN	2143.0	22	3746.0	11	86.0	9	147.0	11	4.0	4.5	12.9	13	5.34
TRIM (5)	203.7	-3	384.4	-11	4.1	61	4.3	-26	2.0	1.2	2.8	65	0.31
BOEING STRAND	371.0	-2	739.0	2	34.0	26	60.0	567	9.2	7.2	26.5	11	3.20
BOEING TECHNOLOGIES	6043.0**	3	11435.0	2	259.0	19	423.0	20	4.3	3.7	19.1	17	6.22
AUTOMOTIVE													
INDUSTRY COMPOSITE	114276.7	7	219685.1	4	5703.2	27	8673.7	-5	5.0	4.2	18.3	10	3.54
CARS & TRUCKS													
GROUP COMPOSITE	100567.8	8	193073.3	4	5113.2	31	7629.6	-6	5.1	4.2	19.6	8	4.19
CHRYSLER	15289.0	27	29782.0	18	1037.0	668	2042.0	181	6.8	1.1	30.0	6	4.51
FORD MOTOR	37937.0	4	74198.0	4	1903.0	21	2556.0	-18	5.0	4.3	13.1	11	2.92
GENERAL MOTORS	44772.4**	6	84012.2	0	2095.5	1	2896.2	-28	4.7	4.9	21.9	8	5.97
MAZDA INTERNATIONAL (2)	1469.0	-10	2886.0	-5	26.0	-43	48.0	-30	1.8	2.8	17.8	7	1.55
TOYOTA	1100.5	-13	2195.1	-10	51.7	21	87.4	-27	4.7	5.1	17.3	8	5.68
PARTS & EQUIPMENT													
GROUP COMPOSITE	9791.6	8	18897.6	7	356.8	-6	620.1	-8	3.6	4.2	2.3	NM	0.22
AMERICAN INDUSTRIES	583.3	14	1094.9	9	14.1	171	20.0	160	2.4	1.0	7.5	15	1.34
BOEING-WARNER AUTOMOTIVE	381.8	7	730.7	7	21.8	4	34.1	-12	5.7	5.9	11.5	13	2.96
GENERAL ENGINE	1316.0	-3	2632.0	-2	44.0	-36	93.0	-32	3.3	5.1	15.0	9	4.50
MAZDA	2069.5	3	4105.7	3	91.5	3	170.2	15	4.4	4.4	24.2	9	3.05
DETROIT DIESEL	491.3	-11	970.1	-10	-16.2	NM	-7.9	NM	NM	2.3	2.4	62	0.30
GENERAL (5)	185.2	-1	367.4	3	12.6	10	21.9	14	6.8	6.1	18.8	16	1.61
GENERAL-PICHER INDUSTRIES (1)	235.1	4	443.7	5	16.8	0	28.3	-5	7.1	7.4	NM	NM	-85.65
GENERAL (4)	839.6	13	1572.0	13	42.9	-10	66.3	-14	5.1	6.4	15.4	14	2.39
GENERAL INDUSTRIES	274.1	73	424.8	32	8.1	98	12.9	25	2.9	2.6	13.7	9	1.77
GENERAL-MOGUL	536.4	6	1058.3	3	15.8	11	26.4	-7	2.9	2.8	-4.6	NM	-0.58
GENERAL (1)	378.0	-18	746.3	-16	14.1	-14	2.4	-90	3.7	3.5	70.4	26	0.52
GENERAL	1618.7	42	3024.5	38	50.1	73	75.9	65	3.1	2.5	20.3	16	2.10
GENERAL MFG. (9)	248.5	4	492.7	2	16.4	3	30.2	-15	6.6	6.7	17.1	13	2.04
GENERAL (A.O.)	428.7	7	854.9	8	18.7	-6	36.1	-6	4.4	5.0	14.7	8	2.82
GENERAL MOTOR PRODUCTS	205.3	12	379.7	10	6.1	-27	10.4	-15	3.0	4.5	6.5	14	1.09
TIRE & RUBBER													
GROUP COMPOSITE	3917.2	0	7714.1	0	233.2	4	423.9	5	6.0	5.7	17.7	11	3.21
GENERAL	188.9	3	359.2	2	20.1	-19	36.0	-19	10.6	13.6	21.6	13	3.59
GENERAL TIRE & RUBBER	398.9	7	779.9	6	25.2	2	48.3	-7	6.3	6.6	13.9	14	1.31
GENERAL TIRE & RUBBER	3329.5	-1	6575.0	0	187.9	8	339.7	11	5.6	5.2	18.7	10	4.19

1 Second quarter ended May 31. (2) Second quarter ended Apr. 30. (3) Third quarter and most recent six months ended June 30. (4) Third quarter and most recent six months ended May 31. (5) Third quarter and most recent six months ended Apr. 30. (6) Fourth quarter and most recent six months ended June 30. (7) Fourth quarter and most recent six months ended May 31. (8) Fourth quarter and most recent six months ended Apr. 30. (9) First quarter and most recent six months ended June 30. (10) First quarter and most recent six months ended May 31. (11) First quarter and most recent six months ended Apr. 30. *Sales include excise taxes. **Sales include other income. ***Sales include excise taxes and other income. 1 Revenues from major subsidiaries not included in consolidated sales. Earnings per share are for latest 12 months, not necessarily for end of most recent fiscal year. 2 include all common-stock equivalents but exclude extraordinary items. NA = not available. NM = not meaningful.

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-19	1 MON. EARN. PER SHA
	2ND QUARTER 1996 \$ MIL.	CHANGE FROM 1995	6 MONTHS 1996 \$ MIL.	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL.	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL.	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
3 BANKS													
INDUSTRY COMPOSITE	67603.0	9	132948.0	9	9240.0	22	16625.4	15	13.7	12.2	16.5	12	4.3
(A) BANKS - EAST													
GROUP COMPOSITE	31687.0	6	62649.2	7	3984.2	23	6752.8	12	12.6	10.8	15.8	12	4.6
BANK OF BOSTON	1325.1**	-1	2586.2	-3	178.0	33	295.0	14	13.4	10.0	16.9	10	4.8
BANK OF NEW YORK	1724.0**	32	3047.0	20	278.0	23	521.0	19	16.1	17.4	19.2	10	4.8
BANKERS TRUST NEW YORK	2080.0**	10	4026.0	13	151.0	66	289.0	NM	7.3	4.8	12.2	11	6.1
CHASE MANHATTAN	6720.0**	1	13652.0	6	856.0	17	767.0	-44	12.7	11.0	15.2	13	5.3
CITICORP	8016.0	1	15935.0	2	952.0	12	1866.0	11	11.9	10.8	19.3	11	7.3
FIRST EMPIRE STATE	289.1**	9	569.1	12	38.7	23	74.8	28	13.4	11.9	17.9	12	20.9
FIRST MARYLAND BANCORP	224.4**	1	457.5	5	32.5	12	62.6	9	14.5	13.1	10.1	NA	N
FLEET FINANCIAL GROUP	2025.4**	1	3882.4	0	277.7	9	541.5	13	13.7	12.6	9.6	23	1.7
MBNA	765.9**	23	1485.7	28	103.3	34	195.5	34	13.5	12.3	30.2	16	1.7
MELLON BANK	1151.0	4	2328.0	6	179.0	4	358.0	5	15.6	15.5	19.7	11	4.8
MORGAN (J.P.)	3900.0**	18	7800.0	16	440.0	40	879.0	54	11.3	9.5	15.5	11	7.8
PNC BANK	1537.0**	2	3079.5	0	248.1	28	486.4	30	16.1	12.3	10.9	19	1.9
REPUBLIC NEW YORK	815.1**	16	1588.1	12	103.1	829	202.6	106	12.6	1.6	14.7	9	6.5
STATE STREET BOSTON	665.3**	10	1318.0	11	71.5	14	141.3	21	10.7	10.3	17.4	15	3.2
SUMMIT BANCORP.	448.7	4	894.7	6	75.4	29	73.1	-37	16.8	13.6	9.1	14	2.4
(B) BANKS - MIDWEST													
GROUP COMPOSITE	14569.9	8	28997.8	9	2198.9	21	4128.6	16	15.1	13.5	17.4	12	3.2
BANC ONE	2488.1**	13	4975.7	14	354.0	15	700.8	15	14.2	13.9	15.3	11	3.1
BOATMEN'S BANCSHARES	929.1**	2	1860.2	5	146.1	14	257.2	18	15.7	14.0	16.3	12	3.4
COMERICA	763.0	2	1554.8	3	118.2	16	234.8	17	15.5	13.0	16.5	11	3.8
FIFTH THIRD BANCORP	435.4**	21	842.1	20	83.2	22	162.4	21	19.1	19.0	18.3	16	3.1
FIRST BANK SYSTEM	1024.6	24	2062.7	26	254.1	84	430.9	59	24.8	16.6	22.3	11	5.3
FIRST CHICAGO NBD	2565.0**	3	5183.0	0	361.0	9	701.0	5	14.1	12.5	18.6	11	3.5
FIRST OF AMERICA BANK	511.3**	-6	1032.5	-4	62.3	10	121.9	17	12.2	10.4	13.9	11	4.0
FIRSTAR	447.1**	3	894.7	5	70.2	30	107.3	19	15.7	12.3	16.2	14	3.2
HUNTINGTON BANCSHARES	442.3	6	884.7	8	65.1	12	127.9	13	14.7	13.9	17.1	12	1.9
MARSHALL & ILSLEY	356.6**	7	702.8	8	50.4	9	96.5	5	14.1	13.9	15.5	13	2.0
MERCANTILE BANCORPORATION	408.5	6	793.0	4	65.1	12	69.6	-39	15.9	15.1	11.4	14	3.2
NATIONAL CITY	1209.5**	5	2390.2	7	182.8	20	359.7	18	15.1	13.2	21.0	11	3.1
NORTHERN TRUST	481.3**	9	953.9	11	63.4	19	124.9	22	13.2	12.1	17.5	14	4.1
NORWEST	2221.6	21	4302.6	22	285.4	22	556.8	23	12.8	12.8	19.0	12	2.9
OLD KENT FINANCIAL	286.6**	7	564.9	8	37.6	0	76.8	7	13.1	13.9	14.4	13	3.0
(C) BANKS - SOUTH & SOUTHEAST													
GROUP COMPOSITE	11645.9	9	23199.0	11	1705.8	19	3166.5	16	14.6	13.4	16.5	12	4.2
BANPONCE	350.8**	15	692.2	18	46.1	35	91.2	35	13.1	11.2	15.5	8	2.8
CENTRAL FIDELITY BANKS	216.0**	3	434.3	5	28.8	11	56.8	10	13.3	12.4	13.4	12	1.8
CRESTAR FINANCIAL	412.0	8	812.4	9	56.7	9	112.1	11	13.8	13.6	13.7	13	4.3
FIRST TENNESSEE NATIONAL	355.7	12	709.9	14	42.3	4	79.8	6	11.9	12.9	19.4	12	2.8
FIRST UNION	2963.1**	16	5793.1	16	439.4	21	682.2	-4	14.8	14.3	17.9	13	4.9
NATIONSBANK	4240.0**	5	8595.0	11	605.0	30	1195.0	31	14.3	11.6	17.5	11	7.8
REGIONS FINANCIAL	401.1**	11	785.7	12	61.5	23	114.3	14	15.3	13.9	13.7	12	3.7
SOUTHERN NATIONAL	460.7	1	912.1	6	73.9	28	143.5	215	16.0	12.7	17.4	11	2.6
SUNTRUST BANKS	998.6**	7	1992.8	3	152.1	8	302.5	9	15.2	15.1	13.4	14	2.6
UNION PLANTERS	256.7**	4	512.9	7	40.6	12	79.8	11	15.8	14.8	15.4	10	2.9
WACHOVIA	991.3**	8	1958.7	11	159.4	-2	309.2	1	16.1	17.8	16.3	12	3.5
(D) BANKS - WEST & SOUTHWEST													
GROUP COMPOSITE	9700.1	20	18101.9	15	1351.1	25	2577.6	21	13.9	13.3	17.1	11	6.3
BANCORP HAWAII	286.7	11	555.4	8	34.6	21	67.3	19	12.1	11.1	12.6	11	3.1
BANKAMERICA	5446.0	-	10809.0	9	723.0	12	1443.0	15	13.3	12.6	14.9	11	7.0
FIRST SECURITY	811.1	7	1414.8	5	42.9	18	79.2	10	13.6	12.3	12.4	16	1.6
U. S. BANCORP	740.7**	-	1471.5	3	127.1	34	240.0	24	17.2	13.5	16.9	14	2.4
UNIONBANCAL	414.7	15	794.2	15	60.5	47	121.1	47	14.6	11.5	16.0	8	5.9
WELLS FARGO	2497.0**	86	3857.0	48	363.0	56	627.0	35	14.5	17.3	30.8	11	19.8
4 CHEMICALS													
INDUSTRY COMPOSITE	38164.6	-1	74259.6	-1	3369.1	-1	6448.6	-6	8.8	8.8	26.3	13	3.2
AIR PRODUCTS & CHEMICALS (3)	997.0	1	2010.0	2	98.0	-2	233.0	23	9.8	10.2	16.0	14	3.7
ALBEMARLE	196.0	39	466.2	26	14.6	17	130.3	381	7.5	3.9	29.1	6	2.8
ARCADIAN	344.3	4	641.7	-7	51.6	139	92.7	155	15.0	6.0	48.0	6	3.2
ARCO CHEMICAL	959.0	-17	1941.0	-15	81.0	-46	187.0	-32	8.4	13.1	21.0	11	4.3
CABOT (3)	457.3	-8	948.6	-3	35.7	-24	78.6	-16	7.8	9.5	26.3	11	2.2
CYTEC INDUSTRIES	318.1	-5	622.6	-3	25.4	13	48.0	7	8.0	6.8	82.3	15	1.8
DEXTER	285.7	1	562.9	-	14.4	20	25.5	14	5.0	4.2	12.1	16	1.8
DOW CHEMICAL	5176.0**	6	10158.0	-	546.0	63	1022.0	14	10.5	6.1	26.8	9	7.8
DUPONT	11148.0***	1	21917.0	2	1001.0	7	1880.0	-1	9.0	8.5	36.6	13	5.8
EASTMAN CHEMICAL	1241.0	6	2502.0	-	112.0	-29	224.0	-23	9.0	12.0	32.3	9	6.1
ENGELHARD	783.9**	9	1558.6	10	40.1	9	72.6	13	5.1	5.1	18.5	21	1.0
ETHYL	299.3	33	541.5	18	20.1	55	39.1	13	6.7	5.8	19.2	14	0.6
FLUOR	344.7	3	692.9	-	14.3	-2	27.5	-1	4.2	4.4	13.2	16	1.6
FREEMONT-MCMORAN	242.8	4	499.6	2	13.2	82	34.4	262	5.4	3.1	79.6	9	4.0

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CORPORATE SCOREBOARD

COMPANY	SALES			PROFITS					MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE-EARNINGS RATIO 7/19	MOST RECENT EPS
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
FULLER (H. B.) (1)	320.2	1	623.8	1	8.4	-16	11.1	-31	2.6	3.1	8.8	18	18
GEON	311.8	-13	557.5	-20	10.1	NM	4.5	-66	3.2	NM	11.2	25	0.8
GEORGIA GULF	231.4	-16	439.4	-26	19.3	-62	35.1	-68	8.3	18.4	242.1	10	2
GOODRICH (B. F.)	646.1	8	1250.6	5	37.9	-14	57.8	-7	5.9	7.4	12.6	17	23
GREAT LAKES CHEMICAL	594.9	-7	1131.9	-6	78.0	-1	144.2	-2	13.1	12.2	20.2	13	41
HANNA (M. A.)	537.3	11	1034.8	6	15.7	-19	29.0	-8	2.9	4.0	10.7	16	11
HERCULES	544.9	-11	1047.5	-20	88.2	12	164.4	-2	16.2	12.9	32.1	17	22
INTERNATIONAL FLAVORS & FRAGRANCES	374.4	-5	757.2	-1	29.7	-61	95.9	-34	7.9	19.2	17.6	24	13
INTERNATIONAL SPECIALTY PRODUCTS	185.0	1	370.6	2	22.6	22	42.5	26	12.2	10.2	11.5	13	0.8
LOCTITE	200.3	0	400.5	1	21.1	-12	44.8	-8	10.6	12.0	24.0	19	23
LUBRIZOL	421.4	-4	828.5	-3	38.1	-38	109.3	-1	9.0	14.0	18.0	12	22
LYONDELL PETROCHEMICAL	1239.0	-10	2404.0	-6	15.0	-89	39.0	-85	1.2	9.9	43.6	11	23
MONSANTO	2579.0	4	4883.0	2	365.0	26	625.0	20	14.2	11.7	22.1	20	14
NL INDUSTRIES	263.2	-7	503.6	-6	11.9	-43	25.3	-26	4.5	7.4	NM	7	14
OLIN	824.0	3	1613.4	3	51.7	19	96.7	18	6.3	5.4	17.7	14	68
PRAXAIR	1093.0	39	2183.0	41	81.0	21	98.0	-26	7.4	8.5	14.2	25	11
ROHM & HAAS	1054.0	1	2048.0	1	101.0	16	201.0	21	9.6	8.4	19.3	12	41
SCHULMAN (A.) (4)	254.4	-11	488.1	-9	12.1	-21	19.7	-30	4.8	5.4	9.8	22	11
SCOTTS (3)	248.0	8	499.2	7	7.6	-42	18.2	-32	3.1	5.7	3.4	79	0.8
STERLING CHEMICALS (3)	218.4	-27	409.3	-32	16.4	-73	22.8	-80	7.5	20.0	18.5	13	0.8
TERRA INDUSTRIES	1085.7**	8	1480.4	2	71.5	-16	89.9	-24	6.6	8.5	23.3	7	11
UNION CARBIDE	1559.0	1	3060.0	2	173.0	-24	330.0	-28	11.1	14.8	37.0	7	5
UNIROVAL CHEMICAL (3)	302.1	1	597.7	4	14.7	19	26.4	-75	4.9	4.2	NM	15	0.8
WELLMAN	283.9	-3	584.9	3	11.7	-46	23.4	-47	4.1	7.3	8.2	13	11

5 CONGLOMERATES

INDUSTRY COMPOSITE	42034.6	6	79608.6	8	3100.8	12	5640.5	12	7.4	7.0	21.0	18	3.1
ALCO STANDARD (3)	1059.1	30	NA	NA	43.7	41	NA	NA	4.1	3.8	9.2	NA	3.1
ALLIEDSIGNAL	3347.0	-8	7125.0	1	272.0	20	497.0	17	8.1	6.3	25.7	16	3.1
ANIXTER INTERNATIONAL	611.8	13	1179.2	13	8.1	-9	18.4	-8	1.3	1.6	8.4	18	0.8
DIAL	950.9	9	1858.2	9	30.3	-36	55.1	20	3.2	5.4	-2.5	NM	0.8
GENERAL ELECTRIC	19066.0**	7	36164.0	10	1908.0	11	3425.0	11	10.0	9.7	23.6	20	4.1
HARCOURT GENERAL (2)	844.3**	9	1542.8	7	10.4	-18	27.1	3	1.2	1.6	20.4	20	2.8
ITT INDUSTRIES	2241.0	4	4442.0	-3	68.0	48	108.0	19	3.0	2.0	5.8	NM	0.8
PALL (5)	247.9	14	487.2	19	38.0	13	70.1	17	15.3	15.4	19.2	19	1.1
PITTTWAY	272.4	16	529.8	16	12.5	17	45.8	136	4.6	4.6	14.3	14	3.1
PREMARK INTERNATIONAL	565.7	5	1094.4	3	-17.3	NM	-5.5	NM	NM	3.2	4.1	27	0.8
ROCKWELL INTERNATIONAL (3)	3489.0	6	6911.0	7	229.0	21	441.0	20	6.6	5.8	20.3	14	3.1
TELEDYNE	662.8	-6	1331.5	0	39.9	22	102.4	6	6.0	4.6	38.0	12	2.8
TENNECO	2792.0	27	5517.0	27	161.0	25	317.0	23	5.8	5.9	19.7	12	4.1
TEXTRON	2384.0**	12	4598.0	10	125.0	17	234.0	16	5.2	5.0	15.0	14	5.1
TRW	2728.5	1	5398.5	2	130.5	6	247.5	4	4.8	4.5	20.4	12	6.1
WHITMAN	772.2	5	1430.1	8	41.7	10	57.7	11	5.4	5.2	22.2	18	1.1

6 CONSUMER PRODUCTS

INDUSTRY COMPOSITE	63234.5	6	122981.1	6	5017.8	15	9429.5	12	7.9	7.3	23.8	24	2.1
(A) APPAREL													
GROUP COMPOSITE	7493.3	12	14378.4	8	374.4	66	667.8	45	5.0	3.4	10.8	32	1.1
BROWN GROUP (11)	355.8	0	704.5	2	0.5	NM	4.3	NM	0.1	NM	2.5	42	0.8
FRUIT OF THE LOOM	732.2	1	1238.4	1	47.8	20	60.3	7	6.5	5.5	-23.2	NM	-2.1
JONES APPAREL GROUP	193.3**	24	453.6	30	13.3	24	33.7	23	6.9	6.9	20.9	19	2.1
KELLWOOD (8)	411.3	4	699.8	2	10.4	NM	8.4	NM	2.5	NM	8.6	13	1.1
LIZ CLAIBORNE	500.6	5	1057.2	6	22.7	33	58.6	30	4.5	3.6	14.2	15	1.1
NIKE (7)	1921.3	36	3412.9	35	156.4	38	270.2	29	8.1	8.0	22.8	27	3.1
NINE WEST GROUP (11)	355.1	108	702.7	NA	15.1	7	-3.8	NA	4.2	8.2	5.7	86	0.8
PHILLIPS-VAN HEUSEN (11)	273.7	-3	657.3	3	-6.6	NM	-2.4	NM	NM	NM	-1.1	NM	-0.8
REEBOK INTERNATIONAL	817.6	4	1720.5	0	19.8	-7	68.2	-22	2.4	2.7	16.2	17	1.1
RUSSELL	290.6	8	548.4	6	16.3	31	28.0	13	5.6	4.6	9.0	21	1.1
VF	1221.0	-4	2379.1	3	69.9	7	125.8	2	5.7	5.1	8.5	23	2.1
WESTPOINT STEVENS	421.0	6	804.0	4	8.7	NM	16.7	NM	2.1	NM	NM	NM	0.8
(B) APPLIANCES & HOME FURNISHINGS													
GROUP COMPOSITE	10789.9	12	22771.1	12	194.5	143	445.0	-3	1.8	0.8	9.2	25	1.1
ARMSTRONG WORLD INDUSTRIES	563.2	5	1064.4	3	30.6	-35	66.9	-9	5.4	8.8	-1.6	NM	-0.8
BEST BUY (10)	1637.2	28	4212.7	31	0.4	91	20.2	-38	0.0	0.4	10.1	20	1.1
CIRCUIT CITY STORES (10)	1615.3	16	3868.5	17	16.8	-32	98.8	9	1.0	1.8	16.1	19	1.1
HEILIG-MEYERS (10)	357.9**	12	698.0	13	12.4	-33	15.3	-54	3.5	5.8	6.8	29	0.8
LA-Z-BOY CHAIR (8)	266.8	14	493.2	11	14.0	10	21.8	9	5.3	5.4	11.4	14	2.1
LEGGETT & PLATT	620.0	5	1211.2	4	26.6	-22	64.3	-8	4.3	5.9	17.4	17	1.1
LEVITZ FURNITURE (9)	228.1	6	451.5	7	-11.0	NM	-18.9	NM	NM	NM	NM	NM	0.8
MAYTAG	754.6	-6	1485.9	-8	44.3	NM	60.5	NM	5.9	NM	18.0	19	1.1
PIER 1 IMPORTS (10)	205.3**	16	449.5	11	8.3	NM	20.8	NM	4.0	NM	16.1	17	0.8
SUNBEAM	345.9	12	685.8	6	7.7	37	24.6	41	2.1	3.7	5.4	30	0.8
TANDY	1352.9**	14	2799.8	16	9.3	-76	23.8	-69	0.7	3.2	10.0	18	2.1
TORO (2)	288.6	35	500.1	19	16.8	147	25.3	68	5.8	3.2	22.3	12	2.1
WHIRLPOOL	2272.0**	7	4331.0	6	52.0	0	90.0	-29	2.3	2.5	9.1	21	2.1
ZENITH ELECTRONICS	282.1	-1	519.5	-5	-33.2	NM	-68.5	NM	NM	NM	-32.9	NM	-1.4

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-19	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
BEVERAGES													
GROUP COMPOSITE	19234.1	7	35155.4	7	2099.6	16	3521.1	16	10.9	10.0	32.9	31	1.36
HEUSER-BUSCH	3418.0	5	6185.4	4	353.4	7	628.9	14	10.3	10.1	25.8	19	3.79
OWN-FORMAN (8)	366.0	7	750.5	6	36.2	7	74.3	4	9.9	9.9	25.6	16	2.31
NANDAIGUA WINE (10)	276.5	24	525.9	21	8.5	-20	1.4	-93	3.1	4.8	11.1	14	1.91
CA-COLA	5253.0	6	9447.0	7	1050.0	17	1763.0	15	20.0	18.2	58.0	37	1.29
CA-COLA BOTTLING CONSOLIDATED	213.6	3	385.6	2	9.5	19	10.5	5	4.5	3.9	42.6	20	1.72
CA-COLA ENTERPRISES	2016.0	10	3616.0	10	59.0	28	66.0	35	2.9	2.5	7.3	47	0.74
PSICO	7691.0	6	14245.0	6	583.0	20	977.0	21	7.6	6.7	23.8	30	1.10
PERSONAL CARE													
GROUP COMPOSITE	6021.0	7	11693.3	7	514.2	10	966.7	9	8.5	8.3	27.0	32	1.84
BERTO-CULVER (3)	415.6	16	811.7	19	16.5	21	30.9	20	4.0	3.8	15.6	21	2.11
ON PRODUCTS	1128.7	6	2144.8	5	85.7	7	123.4	8	7.6	7.6	202.1	20	2.18
LGATE-PALMOLIVE	2167.3	4	4221.0	4	148.9	4	292.4	-2	6.9	6.9	8.6	85	0.97
OLAB	373.2	12	706.9	10	27.6	7	47.2	7	7.4	7.8	22.5	19	1.58
LETTE	1745.7	9	3422.6	9	225.3	17	455.2	17	12.9	12.1	33.0	32	2.00
H (8)	190.6	3	386.3	4	10.2	2	17.5	3	5.4	5.4	12.1	12	4.51
TOBACCO													
GROUP COMPOSITE	19696.1	0	38982.9	2	1835.1	2	3829.0	7	9.3	9.1	25.9	15	4.73
ERICAN BRANDS	1382.6	-5	2721.6	-8	122.0	2	246.1	4	8.8	8.2	14.6	15	3.06
LIP MORRIS	13760.0	0	27494.0	2	1621.0	15	3186.0	15	11.8	10.2	41.4	14	7.09
R NABISCO HOLDINGS	4203.0	3	8089.0	6	-27.0	NM	171.0	51	NM	3.8	3.9	27	1.13
T	350.5*	3	678.3	5	119.1	8	225.9	8	34.0	32.3	156.9	14	2.28
CONTAINERS & PACKAGING													
GROUP COMPOSITE	10142.9	-3	19371.7	-3	356.0	-48	731.9	-39	3.5	6.6	14.6	14	1.83
GLASS, METAL & PLASTIC													
GROUP COMPOSITE	4098.1	24	7180.7	18	187.6	37	268.3	18	4.6	4.2	6.0	30	0.90
LL	600.1	-21	1062.1	-22	11.8	-46	17.3	55	2.0	2.9	-7.5	NM	-1.42
OWN CORK & SEAL	2353.7	70	3904.9	55	104.1	99	135.4	53	4.4	3.8	3.7	46	0.94
JENS-ILLINOIS	963.7	-2	1869.5	-2	66.6	13	106.2	15	6.9	6.0	33.0	11	1.51
S. CAN	180.6	9	344.2	8	5.1	28	9.4	4	2.8	2.4	4.9	46	0.32
PAPER													
GROUP COMPOSITE	6044.8	-16	12191.0	-12	168.4	-70	463.6	-52	2.8	7.7	19.6	11	2.20
X TECHNOLOGIES	184.0	9	361.1	11	9.8	12	17.9	23	5.3	5.2	5.4	22	0.82
MIS	411.9	8	797.5	6	25.2	19	46.9	26	6.1	5.5	17.6	19	1.79
YLRD CONTAINER (3)	225.5	-21	444.8	-18	0.1	NM	1.3	-98	0.0	14.0	57.4	5	1.37
PERSON SMURFIT	844.0	-22	1760.0	15	27.0	-59	80.0	-24	3.2	6.1	NM	6	2.00
NGVIEW FIBRE (2)	199.7	-15	408.9	-11	10.0	-55	25.6	-35	5.0	9.6	13.7	13	1.21
AIL-WELL	185.1	43	378.8	49	3.6	51	6.4	30	2.0	1.8	11.6	8	1.10
CK-TENN (3)	216.2	-11	432.7	-8	13.5	24	25.8	19	6.3	4.5	14.0	13	1.54
INOCO PRODUCTS	689.9	0	1359.1	2	46.8	6	90.0	10	6.8	6.4	21.6	16	1.82
ONE CONTAINER	1282.3	-35	2603.8	-31	-21.1	NM	11.3	-95	NM	6.7	24.5	6	2.25
MPLE-INLAND	872.1	-2	1732.0	0	35.4	-51	81.8	-38	4.1	8.2	11.6	12	4.14
ION CAMP	934.0	-16	1912.3	-10	18.1	-86	76.6	-68	1.9	12.0	13.5	12	4.16
DISCOUNT & FASHION RETAILING													
GROUP COMPOSITE	99585.3	11	223959.6	12	1726.0	15	4350.2	-29	1.7	1.7	10.2	28	0.94
ES DEPARTMENT STORES (11)	438.7**	0	1107.7	-3	-7.0	NM	4.2	-78	NM	NM	3.3	19	0.13
ITOZONE (4)	524.2	23	950.0	20	37.6	16	64.9	15	7.2	7.6	21.4	31	1.03
IKER (J.) (11)	195.5	-16	466.8	-13	0.8	29	1.5	-79	0.4	0.3	-20.8	NM	-2.77
ARNES & NOBLE (11)	508.8	27	1231.3	24	-5.4	NM	-47.0	NM	NM	NM	-13.4	NM	-1.61
EST PRODUCTS (11)	269.8	-1	854.5	-2	-34.6	NM	-109.3	NM	NM	NM	-55.5	NM	-3.89
RDERS GROUP (11)	404.0	14	1073.5	18	-3.4	NM	-16.0	NM	NM	NM	-44.3	NM	-4.83
ADLEES (11)	340.5**	-11	919.6	-14	-53.7	NM	-162.6	NM	NM	NM	NM	NM	-20.04
LDOR (11)	568.6	1	1507.6	0	-43.3	NM	-297.4	NM	NM	NM	NM	NM	-19.30
ARSON PIRIE SCOTT (11)	236.8**	5	601.6	-6	9.7	-72	33.1	-55	4.1	13.8	12.4	10	2.38
JW COMPUTER CENTERS	218.7	50	425.4	48	8.5	97	14.0	65	3.9	3.0	21.3	39	1.19
FARMING SHOPS (11)	237.5	-3	559.3	-5	-6.2	NM	-113.2	NM	NM	NM	-34.0	NM	-1.37
NSOLIDATED STORES (11)	343.2	18	881.1	18	3.6	20	46.1	12	1.1	1.0	16.3	26	1.33
ORPORATE EXPRESS (10)	500.6	52	969.1	61	9.6	48	-10.3	NM	1.9	2.0	1.2	NM	0.07
AYTON HUDSON (11)	5380.0**	13	13330.0	13	41.0	273	269.0	-7	0.8	0.2	9.3	21	1.48
LARD DEPARTMENT STORES (11)	1501.8**	9	3463.1	10	56.4	17	85.5	-49	3.8	3.5	6.9	21	1.55
JLLAR GENERAL (11)	455.9	22	1031.2	20	15.0	22	53.6	19	3.3	3.3	20.5	26	1.03
ISON BROTHERS STORES (11)	258.1	-19	674.9	-12	-17.7	NM	-124.3	NM	NM	NM	NM	NM	-10.57
BRI-CENTERS OF AMERICA (11)	203.0	11	471.4	7	1.1	285	15.6	9	0.5	0.2	10.5	15	0.95
ILLY DOLLAR STORES (4)	427.9	13	876.2	9	18.8	14	34.7	4	4.4	4.3	13.7	16	1.03
DERATED DEPARTMENT STORES (11)	3300.7**	10	8565.6	40	-37.9	NM	206.9	312	NM	NM	2.2	74	0.42
NGERHUT	449.6	-5	857.8	-3	2.1	-63	0.1	NM	0.5	1.2	7.2	19	0.81
AP (11)	1113.2	31	2635.3	28	81.6	63	236.2	40	7.3	5.9	22.3	23	1.34
ECHINGER (11)	561.3	1	1063.1	-2	-6.0	NM	-87.5	NM	NM	0.2	-21.6	NM	-2.00
ILLS STORES (11)	370.2	2	1070.0	3	-14.7	NM	-7.3	NM	NM	NM	-11.1	NM	-2.70
OME DEPOT (11)	4362.2	22	8114.1	22	195.0	24	380.4	25	4.5	4.4	14.8	32	1.62
OME SHOPPING NETWORK	270.4	10	553.1	13	5.0	NM	7.2	NM	1.8	NM	-24.4	NM	-0.41

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-19	MO'S EARN- ING SHR
	2ND QUARTER 1996 \$ MIL	CHANGE FR. M. 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FR. M. 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FR. M. 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FR. M. 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
INTIMATE BRANDS (11)	586.2	22	1563.3	22	25.2	3	157.2	9	4.3	5.1	77.7	25	0
KMART (11)	7640.0**	2	18249.0	4	-38.0	NM	-407.0	NM	NM	NM	-9.8	NM	-1
KOHLS (11)	468.6	27	1175.7	26	13.8	17	55.8	22	2.9	3.2	17.5	31	1
LANDS' END (11)	211.8	2	611.3	4	4.4	237	30.2	19	2.1	0.6	16.5	21	1
LIMITED (11)	1787.9**	13	4559.3	10	28.2	-28	244.4	-17	1.6	2.5	59.7	7	2
LOWE'S (11)	1906.5	17	3603.2	15	47.1	-20	85.2	-19	2.5	3.6	12.5	25	1
MAY DEPARTMENT STORES (11)	2511.0**	13	6351.0	12	98.0	13	494.0	7	3.9	3.9	17.9	15	2
MERCANTILE STORES (11)	655.4	9	1659.7	8	13.3	33	90.9	31	2.0	1.7	8.6	14	3
MEYER (FRED) (11)	1040.0	11	2006.2	13	9.4	206	28.3	143	0.9	0.3	6.3	21	1
MICHAELS STORES (11)	301.9	14	758.6	18	2.7	-64	4.9	-84	0.9	2.8	-7.5	NM	-1
MICRO WAREHOUSE	437.2	15	951.6	25	5.4	51	2.2	-91	1.2	2.9	7.3	21	0
NEIMAN MARCUS GROUP (5)	474.1**	14	1099.5	9	18.8	70	41.6	15	4.0	2.7	65.4	23	1
NORDSTROM (11)	940.5**	11	2214.8	8	27.3	-1	81.5	-16	2.9	3.3	11.4	20	2
OFFICE DEPOT	1381.4	15	3014.4	18	28.2	3	61.7	3	2.0	2.3	12.8	16	0
OFFICEMAX (11)	730.6	31	1553.8	38	12.6	56	41.4	69	1.7	1.4	13.1	13	1
PAYLESS CASHWAYS (11)	682.3	4	1209.0	-5	5.9	27	-1.8	NM	0.9	0.6	-51.4	NM	-3
PAYLESS SHOESOURCE (11)	601.4	6	1153.0	NA	24.2	-9	-8.2	NA	4.0	4.7	6.6	NA	
PENNEY (J.C.) (11)	4452.0**	2	11084.0	1	142.0	-9	468.0	-20	3.2	3.6	14.1	15	3
PEP BOYS-MANNY, MOE & JACK (11)	428.6	19	839.1	20	20.1	24	38.7	12	4.7	4.5	12.5	22	1
PETSMART (11)	310.2	23	602.4	19	0.9	NM	16.2	NM	0.3	NM	-0.8	NM	-0
PRICE/COSTCO (4)	4311.5**	11	9000.2	10	41.3	27	112.7	16	1.0	0.8	13.9	18	1
PROFFITT'S (11)	296.6**	3	741.2	4	6.3	71	-13.2	NM	2.1	1.3	-1.8	NM	-0
ROSS STORES (11)	370.9	25	818.0	19	13.9	260	35.1	115	3.8	1.3	17.4	15	2
SAKS HOLDINGS (11)	464.5**	21	1005.5	22	-3.0	NM	24.9	79	NM	NM	-55.4	NM	-1
SEARS, ROEBUCK	9132.0	11	17127.0	9	274.0	26	425.0	24	3.0	2.7	25.9	16	2
SERVICE MERCHANDISE	860.0	-1	1575.6	-2	-1.8	NM	26.5	NM	NM	0.1	12.7	11	0
SHOPKO STORES (10)	610.9	9	1109.3	6	5.8	7	26.8	11	0.9	1.0	9.2	13	1
SPIEGEL	668.6	-4	1303.3	-4	-3.3	NM	-17.6	NM	NM	NM	-0.5	NM	-0
SPORTS AUTHORITY (11)	271.1	22	595.6	21	2.1	22	15.2	22	0.8	0.8	8.1	31	0
STAPLES (11)	916.8	37	1892.3	42	13.0	65	47.9	64	1.4	1.2	12.5	32	0
STRAWBRIDGE & CLOTHIER (11)	208.1**	5	546.0	0	-6.9	NM	6.7	53	NM	NM	-4.1	NM	-0
TALBOTS (11)	236.2	2	535.0	8	20.8	-4	34.1	12	8.8	9.4	15.3	17	1
TIFFANY (11)	180.7**	20	461.4	19	5.1	135	30.6	42	2.8	1.4	15.2	26	1
TJX (11)	1604.2	93	3359.7	81	30.1	216	42.6	92	1.9	1.1	14.9	31	0
TOYS 'R' US (11)	1645.5	10	6250.7	10	18.7	1	111.7	-74	1.1	1.2	4.3	48	0
U.S. OFFICE PRODUCTS (8)	242.6	116	NA	NA	4.2	491	NA	NA	1.7	0.6	3.6	79	0
VALUE CITY DEPARTMENT STORES (5)	207.6**	13	504.0	10	0.9	NM	17.1	34	0.4	NM	6.7	22	0
VENTURE STORES (11)	351.2**	20	937.7	-18	1.7	NM	15.0	-29	0.5	NM	-7.2	NM	-1
WABAN (11)	974.6	10	2050.7	10	9.5	15	35.3	19	1.0	0.9	13.0	9	2
WAL-MART STORES (11)	22772.0	11	50322.0	12	571.0	3	1513.0	-4	2.5	2.7	18.1	20	1
WICKES LUMBER	228.8	-16	381.3	-18	1.9	-24	-4.3	NM	0.8	0.9	-85.9	NM	-2
WOOLWORTH (11)	1820.0	1	4257.0	-1	-22.0	NM	-129.0	NM	NM	NM	-8.8	NM	-0
ZALE (5)	222.3	16	674.2	9	-2.4	NM	43.8	16	NM	NM	9.2	15	1

9 ELECTRICAL & ELECTRONICS

INDUSTRY COMPOSITE	40214.9	6	79300.2	9	2995.7	-15	6081.1	-9	7.5	9.3	17.9	16	2.7
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(A) ELECTRICAL PRODUCTS

GROUP COMPOSITE	5769.4	6	11318.2	7	409.3	25	751.2	35	7.1	6.0	19.2	15	2.9
AMETEK	224.0	2	451.6	5	13.0	9	25.2	14	5.8	5.4	53.8	14	1.4
COOPER INDUSTRIES	1380.1**	9	2694.2	13	88.3	7	150.4	9	6.4	6.5	16.4	14	2.7
EATON	1782.0	1	3518.0	1	103.0	-6	198.0	-9	5.8	6.3	18.5	11	4.8
GENERAL SIGNAL	515.0	15	996.7	13	31.6	29	57.0	8	6.1	5.5	16.7	18	2.1
HUBBELL	328.9	12	633.5	10	35.7	19	67.4	15	10.9	10.2	19.1	18	3.9
NATIONAL SERVICE INDUSTRIES (4)	516.9	2	999.1	3	27.7	8	46.9	9	5.4	5.1	13.4	18	2.0
RAYCHEM (6)	432.2	-	850.0	9	48.7	NM	90.4	NM	11.3	NM	17.6	20	3.2
THOMAS & BETTS	349.4	17	691.1	15	23.4	21	42.8	18	6.7	6.5	14.1	16	2.1
UCAR INTERNATIONAL	241.0	6	484.0	11	38.0	41	73.0	NM	15.8	11.9	NM	15	2.4

(B) ELECTRONICS

GROUP COMPOSITE	17520.3	6	33839.5	8	942.9	-19	1986.0	-8	5.4	7.1	14.0	20	2.5
ANDREW (3)	197.2	16	380.4	14	24.0	27	42.3	28	12.2	11.1	21.1	34	1.3
GENERAL INSTRUMENT	675.2	10	1291.0	6	-58.1	NM	-26.9	NM	NM	8.8	-1.5	NM	-0.1
HARRIS (6)	1012.0	10	1887.9	6	60.3	14	104.5	15	6.0	5.7	13.0	12	4.5
HUGHES ELECTRONICS	4032.6	9	7646.2	5	306.6	6	618.3	11	7.6	7.8	13.1	20	2.9
LITTON INDUSTRIES (5)	1004.4	17	1743.9	12	38.8	9	71.6	11	3.9	4.1	16.8	14	3.0
MOTOROLA	6835.0	-1	13790.0	7	326.0	32	710.0	-17	4.8	7.0	13.9	20	2.7
QUALCOMM (3)	234.9	136	384.1	103	1.5	79	3.0	-78	0.6	7.3	2.9	NM	0.3
RAYTHEON	3111.9	11	5881.3	13	209.4	7	395.9	7	6.7	6.9	18.8	14	3.4
VARIAN ASSOCIATES (3)	417.1	6	834.7	1	34.4	19	67.4	22	8.2	7.3	29.3	11	3.8

(C) INSTRUMENTS

GROUP COMPOSITE	3152.6	9	6078.4	11	157.9	10	276.3	-5	5.0	5.0	16.5	17	2.1
BECKMAN INSTRUMENTS	265.2	15	490.0	12	19.0	38	32.7	36	7.2	6.0	16.3	17	1.9
HONEYWELL	1771.6	7	3391.1	8	83.3	21	148.4	20	4.7	4.2	17.7	18	2.8
PERKIN-ELMER (6)	305.4	9	674.4	9	9.5	NM	-26.4	NM	3.1	NM	4.3	NM	0.3
TEKTRONIX (7)	490.7	11	924.2	13	28.2	16	50.6	11	5.7	5.5	14.7	13	3.0
TERADYNE	319.7	12	668.7	29	17.9	-54	71.1	12	5.6	13.6	19.9	6	1.9

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE EARNINGS RATIO 7-19	12 MONTHS EARNINGS PER SHARE
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
) SEMICONDUCTORS & OTHER COMPONENTS													
GROUP COMPOSITE	13772.5	4	28064.2	11	1485.5	-22	3067.6	-17	10.8	14.3	21.4	15	2.83
APTEC (9)	202.0	46	398.0	48	17.9	-43	59.0	3	8.9	22.6	17.6	25	1.64
ADVANCED MICRO DEVICES	455.1	29	999.3	21	-34.7	NM	-9.3	NM	NM	12.6	4.8	11	0.97
ADAPTEC	1365.5	2	2728.5	4	115.6	19	232.1	14	8.5	7.3	16.2	18	2.09
APHENOL	198.9	-4	393.7	-3	17.4	8	34.3	13	8.8	7.7	18.5	14	1.42
ALOG DEVICES (2)	303.3	32	584.1	33	44.0	53	84.1	61	14.5	12.5	20.2	16	1.24
MEL	268.7	84	508.8	92	50.3	105	95.2	115	18.7	16.8	26.8	16	1.64
X (9)	268.2	-12	561.1	-1	32.5	7	69.2	37	12.1	10.0	22.4	11	1.60
RRUS LOGIC (9)	214.9	-28	448.0	-22	-7.6	NM	-96.0	NM	NM	7.6	-15.5	NM	-1.03
TEL	4621.0	19	9265.0	24	1041.0	18	1935.0	9	22.5	22.6	26.9	17	4.22
BIL CIRCUIT (4)	219.7	66	455.3	84	6.2	405	12.6	NM	2.8	0.9	20.5	9	1.30
I LOGIC	325.4	6	636.7	8	46.5	-17	88.8	-12	14.3	18.2	17.8	11	1.71
RON TECHNOLOGY (4)	771.0	1	1767.5	27	58.2	-74	246.4	-39	7.5	28.9	34.6	5	3.96
ATIONAL SEMICONDUCTOR (7)	612.4	-9	1212.7	-2	9.1	-89	32.1	-77	1.5	12.1	11.4	11	1.36
AD-RITE (3)	238.3	-6	496.5	0	-22.9	NM	-21.6	NM	NM	12.8	13.1	7	1.39
ELECTRON (4)	680.6	32	1337.7	35	27.7	36	55.4	44	4.1	3.9	16.0	16	2.08
XAS INSTRUMENTS	2845.0	-12	5921.0	-3	76.0	-73	239.0	-53	2.7	8.6	19.1	10	4.21
SI TECHNOLOGY	182.5	-1	350.2	1	8.3	539	11.4	-1	4.5	0.7	8.8	12	0.98
D FOOD													
INDUSTRY COMPOSITE	72259.4	6	140753.8	6	1329.5	-43	3441.5	-25	1.8	3.4	18.9	24	1.53
J FOOD DISTRIBUTION													
GROUP COMPOSITE	8381.7	3	15319.0	3	52.3	-30	120.4	-19	0.6	0.9	10.6	17	1.48
INTERNATIONAL MULTIFOODS (10)	626.1	-1	1261.3	1	-0.4	NM	5.3	-67	NM	0.7	6.4	16	1.06
ASH FINCH	735.2**	9	1419.7	9	6.1	4	8.9	4	0.8	0.9	8.2	10	1.63
CHFOOD HOLDINGS (8)	999.6	11	1766.4	6	15.4	33	19.2	-12	1.5	1.3	19.7	27	1.26
KOFF-SEXTON (8)	474.8	14	927.2	17	-22.8	NM	-22.3	NM	NM	0.6	-7.8	NM	-1.12
MART & FINAL	307.4	12	589.7	12	6.3	99	10.5	58	2.0	1.2	15.4	22	1.06
PER FOOD SERVICES (4)	259.9**	-1	528.7	2	1.9	7	4.2	10	0.7	0.7	6.9	12	0.88
PERVALU (10)	4978.8	0	8826.0	0	46.0	0	94.7	6	0.9	0.9	13.8	12	2.46
K FOOD PROCESSING													
GROUP COMPOSITE	31254.7	8	60543.7	7	825.3	-53	2165.9	-34	2.6	6.1	17.8	25	1.78
AMPELL SOUP (5)	1831.0	5	4048.0	7	145.0	14	402.0	12	7.9	7.3	27.9	21	3.06
ANAGRA (7)	5982.6	3	11758.9	2	-193.7	NM	-65.3	NM	NM	2.6	7.3	54	0.79
PC INTERNATIONAL	2513.7	23	4923.2	23	153.9	8	276.3	9	6.1	7.0	27.5	19	3.60
AN FOODS (7)	739.4	8	1457.4	8	-86.1	NM	-79.4	NM	NM	3.8	-9.8	NM	-1.24
OLE FOOD	1041.2	-3	1855.6	-3	63.6	-16	93.6	-7	6.1	7.1	19.3	21	1.88
ARTHGRAINS (9)	370.5	-4	738.2	-2	0.7	NM	-4.4	NM	0.2	NM	-0.8	NA	NA
ODBRANDS AMERICA	200.7	37	386.7	35	8.7	351	10.8	191	4.3	1.3	36.8	9	1.34
ENERAL MILLS (7)	1382.1	13	2691.3	10	77.5	NM	193.8	NM	5.6	NM	154.8	18	3.00
ENZ (H.J.) (8)	2536.6	5	4729.7	8	170.2	7	326.7	10	6.7	6.5	26.7	19	1.75
ERSHEY FOODS	796.3	10	1727.9	9	40.8	23	100.3	7	5.1	4.6	25.9	20	3.62
RMEL FOODS (2)	746.7	0	1471.0	-1	24.5	-3	45.2	-26	3.3	3.4	14.0	17	1.37
UDSON FOODS (3)	337.2	10	667.5	16	3.3	-65	5.2	-70	1.0	3.1	7.1	18	0.75
P	3260.3	2	6345.0	2	87.0	1	140.0	2	2.7	2.7	24.5	8	2.92
INTERSTATE BAKERIES (7)	745.7	141	1672.2	150	8.5	50	12.6	45	1.1	1.8	5.3	38	0.70
ELLOGG	1651.4	-7	3437.3	-2	78.1	-43	284.2	-14	4.7	7.6	29.5	36	2.06
McCORMICK (1)	435.7	2	867.5	0	11.0	-31	20.3	-43	2.5	3.6	16.0	21	1.02
ABISCO HOLDINGS	2178.0	6	4168.0	7	-216.0	NM	-163.0	NM	NM	3.8	0.6	NM	0.09
ALGRIM'S PRIDE (3)	294.3	28	566.3	27	1.0	-84	0.5	NM	0.3	2.7	0.9	NM	0.05
IONEER HI-BRED INTERNATIONAL (4)	1168.0	11	1449.0	9	303.0	11	307.0	9	25.9	25.9	19.0	20	2.51
AKER OATS	1481.8	-7	2704.6	-16	64.6	-81	96.8	-86	4.4	21.7	9.9	40	0.79
MITHFIELD FOODS (8)	873.8	129	1560.8	90	7.0	115	17.8	-17	0.8	0.9	10.0	23	1.06
UNIVERSAL FOODS (3)	200.8	-3	400.8	0	15.7	8	30.3	7	7.8	7.0	12.8	17	1.78
RIGLEY (WM.) JR.	486.9**	2	916.8	3	57.0	-11	114.7	-4	11.7	13.4	26.5	26	1.89
L FOOD RETAILING													
GROUP COMPOSITE	32623.0	5	64891.1	6	451.9	-12	1155.1	1	1.4	1.7	24.1	22	1.18
LBERTSON'S (11)	3343.9	8	6622.8	8	112.4	13	266.5	9	3.4	3.2	23.6	21	1.90
ERICAN STORES (11)	4580.0	5	9670.6	7	64.2	19	185.8	1	1.4	1.2	13.7	16	2.23
RUNO'S (11)	752.7	12	1401.3	7	4.2	-64	16.5	-32	0.6	1.8	6.1	30	0.45
ASEY'S GENERAL STORES (8)	236.9***	15	459.8	13	3.2	0	10.1	13	1.4	1.6	13.2	18	1.02
AGLE FOOD CENTERS (11)	248.1	1	531.0	5	1.0	NM	-5.2	NM	0.4	NM	-52.5	NM	-1.13
ODD LION	2084.4	10	4108.9	9	48.6	25	89.4	17	2.3	2.0	16.4	21	0.40
ENERAL NUTRITION (11)	230.2	20	496.2	18	20.2	34	43.2	42	8.8	7.9	22.7	16	0.85
ANT FOOD (10)	895.6	3	2159.8	4	25.8	17	70.6	13	2.9	2.5	12.6	19	1.78
REAT ATLANTIC & PACIFIC TEA (10)	3092.6	-1	5423.6	-1	21.9	50	47.4	133	0.7	0.5	7.8	17	1.69
ANNAFORD BROTHERS	729.1	15	1419.6	15	19.5	3	34.2	2	2.7	3.0	13.4	19	1.68
ASH N' KARRY FOOD STORES (5)	256.4	-5	537.8	-1	3.6	34	4.8	NA	1.4	1.0	-3.9	NA	NA
ROGER	5844.4	3	11628.6	5	78.4	5	154.9	5	1.3	1.5	NM	15	2.55
ENN TRAFFIC (11)	827.7**	-4	1775.4	3	-9.0	NM	-36.7	NM	NM	0.0	NM	NM	-8.16
UALITY FOOD CENTERS	184.4	5	361.0	15	6.2	17	10.9	20	3.3	3.0	43.8	19	1.51
UDDICK (3)	532.6	4	1054.9	5	13.6	20	23.1	8	2.6	2.2	12.0	14	0.87
AFEWAY	3945.4	5	7828.1	6	106.7	55	203.1	55	2.7	1.8	44.4	21	1.68
MITH'S FOOD & DRUG CENTERS	690.0	-10	1383.2	-9	-132.9	NM	-134.1	NM	NM	1.2	NM	NM	-8.13

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-19	12 MON. EARN PER SHA
	2ND QUARTER 1996 \$ MIL.	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL.	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL.	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL.	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
STOP & SHOP (11)	1513.8	27	2613.0	24	27.5	6	46.7	-4	1.8	2.2	21.6	22	1.9
SUPERMARKETS GENERAL HOLDINGS (11)	961.2	-7	2083.3	-2	-5.3	NM	44.7	273	NM	0.1	NM	NA	NM
VONS	1261.0	11	2466.6	8	22.7	57	40.2	41	1.8	1.3	11.9	20	1.8
WEIS MARKETS	432.6	6	865.8	8	19.4	6	39.1	4	4.5	4.5	10.2	17	1.9

11 FUEL

INDUSTRY COMPOSITE	123974.0	10	241266.5	10	7159.9	46	13928.5	40	5.8	4.4	13.6	19	3.1
(A) COAL, OIL & GAS GROUP COMPOSITE	117609.2	9	228965.6	10	6729.5	47	13133.6	40	5.7	4.3	13.8	18	3.3
AMERADA HESS	2543.8**	43	4776.3	27	376.4	NM	442.4	NM	14.8	NM	2.3	77	0.6
AMOCO	7831.0	15	15108.0	12	600.0	13	1328.0	26	7.7	7.8	14.0	16	4.3
APACHE	223.7**	10	429.5	16	24.4	NM	40.1	768	10.9	0.3	5.0	46	0.7
ASHLAND (3)	3249.0	8	6095.0	10	80.0	67	78.0	311	2.5	1.6	7.8	21	1.7
ATLANTIC RICHFIELD	4559.0	13	8715.0	10	434.0	11	804.0	13	9.5	9.7	21.3	13	8.9
BURLINGTON RESOURCES	296.0	40	551.0	29	48.0	NM	86.0	NM	16.2	0.9	-8.6	NM	1.5
CHEVRON	10514.0*	12	20671.0	13	872.0	44	1488.0	40	8.3	6.5	8.9	28	2.0
COASTAL	2938.0	12	6033.1	15	66.1	16	148.6	29	2.3	2.2	10.4	16	2.7
CROWN CENTRAL PETROLEUM	431.2	13	802.3	11	3.0	-57	-10.0	NM	0.7	1.9	-43.9	NM	-7.9
DIAMOND SHAMROCK	1231.4***	25	2402.5	31	18.7	-33	25.9	-22	1.5	2.9	5.6	25	1.2
ENRON OIL & GAS	197.1**	7	356.1	5	47.6	-1	73.5	-5	24.2	26.2	11.7	31	0.8
EXXON	28561.0**	0	56456.0	2	1570.0	-4	3455.0	5	5.5	5.7	15.9	16	5.3
LOUISIANA LAND & EXPLORATION	246.0	18	508.5	27	17.2	169	37.8	282	7.0	3.1	11.8	43	1.3
MITCHELL ENERGY & DEVELOPMENT (11)†	233.9	9	430.8	-2	23.2	NM	-19.8	NM	9.9	NM	12.8	16	1.2
MOBIL	19548.0**	4	38248.0	5	783.0	337	1519.0	86	4.0	1.0	16.9	15	7.6
MURPHY OIL	518.4**	16	955.6	11	28.1	37	52.1	42	5.4	4.6	-9.3	NM	2.3
NGC	1163.2	38	2810.3	71	13.8	184	44.2	-27	1.2	0.6	13.1	25	0.6
OCCIDENTAL PETROLEUM	2457.0	8	4979.0	8	181.0	-3	345.0	-5	7.4	7.0	11.9	19	1.2
PHILLIPS PETROLEUM	3937.0	10	7532.0	13	221.0	96	916.0	309	5.6	3.1	29.2	9	4.4
QUAKER STATE	301.8	17	580.6	17	7.2	NM	12.9	NM	2.4	NM	5.4	32	0.4
SUN	2961.0***	2	5506.0	0	-3.0	NM	-8.0	NM	NM	4.7	4.8	50	0.5
TEXACO	11261.0**	22	21532.0	18	689.0	154	1075.0	56	6.1	2.9	11.4	21	4.0
TOSCO	2430.7	28	4450.8	24	49.6	140	73.6	347	2.0	1.1	20.8	15	3.5
ULTRAMAR	877.3	25	1613.9	21	28.4	739	43.2	595	3.2	0.5	11.7	14	1.9
UNION PACIFIC RESOURCES GROUP	427.9	25	817.6	23	70.4	-4	129.6	-4	16.5	21.6	25.4	NA	NM
UNION TEXAS PETROLEUM HOLDINGS	223.0	11	481.2	9	31.0	54	78.6	18	13.9	10.0	23.3	15	1.3
UNOCAL	2434.0**	18	4476.0	19	238.0	205	362.0	138	9.8	3.8	17.4	18	1.7
USX-MARATHON GROUP	4071.0*	15	7698.0	12	124.0	15	340.0	84	3.0	3.1	2.3	88	0.2
VALERO ENERGY	1092.2	41	2159.3	47	20.9	2	40.8	68	1.9	2.6	6.2	15	1.4
VASTAR RESOURCES	668.0	36	1426.7	45	53.7	149	109.3	141	8.0	4.4	110.6	20	1.7
ZEIGLER COAL HOLDING	182.7**	4	363.7	-8	12.7	-40	22.8	-16	6.9	11.0	-15.4	NM	0.5
(B) PETROLEUM SERVICES GROUP COMPOSITE	6364.8	19	12300.9	19	430.4	35	795.0	34	6.8	6.0	11.7	29	1.7
BAKER HUGHES (3)	765.9	15	1510.7	14	46.9	45	88.4	47	6.1	4.8	10.0	30	1.1
HALLIBURTON	1776.8**	27	3438.2	29	67.1	22	118.6	27	3.8	3.9	14.5	25	2.2
NABORS INDUSTRIES (3)	181.3	19	344.6	16	18.7	43	35.5	40	10.3	8.5	17.0	22	0.7
NOBLE AFFILIATES	183.6**	71	354.0	78	16.9	402	39.5	941	9.2	3.1	9.7	53	0.7
SCHLUMBERGER	2150.8	15	4178.6	15	196.7	18	367.6	17	9.1	8.9	13.4	28	2.8
SMITH INTERNATIONAL	270.3**	31	509.1	26	15.0	48	27.9	33	5.5	4.9	17.5	26	1.3
TIDEWATER (9)	175.9	13	337.1	15	24.4	40	36.5	62	13.9	11.2	11.3	32	1.4
WEATHERFORD ENTERRA	233.8	11	452.6	5	14.9	NM	28.4	151	6.4	NM	0.9	NM	0.1
WESTERN ATLAS	626.5	11	1175.9	10	29.9	23	52.5	21	4.8	4.3	7.7	28	2.0

12 HEALTH CARE

INDUSTRY COMPOSITE	60290.2	10	119553.8	11	6026.5	15	12337.1	10	10.0	9.6	23.4	25	2.1
(A) DRUG DISTRIBUTION GROUP COMPOSITE	17895.2	10	35601.1	10	371.7	24	753.5	14	2.1	1.9	6.3	51	0.5
AMERISOURCE HEALTH (3)	1420.0	23	2782.1	19	10.4	5	20.5	24	0.7	0.9	NM	17	1.7
ARBOR DRUGS (5)	208.2	19	422.7	17	6.1	16	14.8	16	2.9	3.0	15.0	18	1.0
BERGEN BRUNSWIG (3)	2492.2**	16	4946.6	17	19.2	14	39.6	14	0.8	0.8	12.9	15	1.7
BIG B (11)	208.8	7	429.9	11	1.8	-63	-3.9	NM	0.9	2.5	-0.3	NM	-0.0
DRUG EMPORIUM (10)	206.7	25	441.7	28	0.5	2	1.5	-38	0.2	0.3	4.8	24	0.1
ECKERD (11)	1354.6	11	2828.5	12	39.4	29	94.0	25	2.9	2.5	117.7	14	1.5
FAY'S (11)	248.6	6	512.9	5	2.1	39	-6.9	NM	0.8	0.6	-4.4	NM	-0.2
GENOVESE DRUG STORES (11)	200.8	12	358.1	6	1.3	-17	4.3	-24	0.6	0.9	10.5	15	0.6
GENS DRUG STORES (11)	665.4	4	1394.7	4	14.0	6	25.7	-16	2.1	2.1	8.9	17	2.3
McKESSON (9)	3501.5**	5	6983.8	4	30.1	-8	68.1	-6	0.9	1.0	12.5	16	2.8
MELVILLE	1363.5	13	2621.9	12	90.9	173	131.4	114	6.7	2.8	-32.6	NM	-5.3
W.D. S. (7)	1630.7	3	2874.0	6	31.6	-3	56.3	12	1.9	2.1	9.2	21	1.1
WATSON (10)	1405.3	4	2836.3	5	32.7	-15	89.7	-2	2.3	2.8	13.7	16	1.8
WYNN (4)	2988.8	14	6167.9	14	91.6	16	218.4	15	3.1	3.0	18.0	22	1.4
(B) DRUGS & RESEARCH GROUP COMPOSITE	22157.4	9	43946.5	10	3591.8	17	7443.2	5	16.2	15.2	28.1	24	2.6
AMERICAN HOME PRODUCTS	289.6	10	547.7	12	0.7	NM	23.8	NM	0.2	NM	14.0	27	1.5
AMERICAN HOME PRODUCTS	3489.8	6	7136.6	5	391.3	31	880.6	-33	11.2	9.1	21.0	29	1.9
AMERICAN HOME PRODUCTS	571.4	16	1079.3	16	178.7	30	322.3	31	31.3	27.9	33.7	26	2.1

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE-EARNINGS RATIO 7-19	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
STOL-MYERS SQUIBB	3696.0	7	7365.0	9	655.0	8	1381.0	9	17.7	17.6	32.5	23	3.83
VENTECH	228.6**	5	455.9	3	21.7	-42	59.9	-26	9.5	17.0	7.4	50	1.03
Y (ELI)	1698.3	5	3481.6	4	345.7	12	734.9	7	20.4	19.2	23.2	23	2.45
RCK	4908.8	19	9439.2	19	972.1	13	1835.9	14	19.8	20.7	30.5	22	2.90
ZER	2661.0	11	5343.0	13	394.0	27	911.0	25	14.8	13.0	29.5	26	2.72
JNE-POULENC RORER	1346.1	2	2618.5	5	102.2	54	187.2	23	7.6	5.0	14.9	27	2.44
IERING-PLOUGH	1476.6	11	2859.3	12	317.1	15	643.7	15	21.5	20.7	59.6	19	3.09
RNER-LAMBERT	1791.2	0	3620.4	6	213.3	6	462.8	15	11.9	11.2	33.9	18	2.96
HEALTH-CARE SERVICES													
GROUP COMPOSITE	6606.7	19	13048.3	21	330.8	19	653.3	14	5.0	5.0	12.3	28	1.08
VERLY ENTERPRISES	798.3	1	1609.4	1	17.0	19	30.7	-1	2.1	1.8	-1.3	NM	-0.14
PRESS SCRIPTS	184.7	37	353.1	39	6.4	41	12.0	36	3.5	3.3	25.9	29	1.37
ALTH CARE & RETIREMENT	194.3	10	381.9	10	14.6	18	28.6	17	7.5	7.0	14.6	21	1.13
ALTH MANAGEMENT ASSOCIATES (3)	184.4	35	369.2	31	24.2	30	49.1	32	13.1	13.5	21.8	27	0.72
ALTHSOUTH	595.6	19	1176.8	24	59.6	399	97.4	117	10.0	2.4	10.7	35	0.89
TEGRATED HEALTH SERVICES	336.2**	17	663.8	18	15.3	6	29.1	2	4.5	5.0	-5.9	NM	-1.17
NOR CARE (7)	340.1	25	674.5	27	6.4	-70	27.3	-33	1.9	7.9	9.3	33	1.05
ADA HEALTHCORP (4)	557.9**	12	1100.8	17	29.3	33	56.7	35	5.3	4.4	15.7	13	1.69
IFICARE HEALTH SYSTEMS (3)	1205.0**	21	2374.4	24	8.6	-72	40.4	-30	0.7	3.0	12.3	19	3.14
VCOR	176.6	78	339.1	77	8.4	82	16.1	83	4.8	4.7	7.3	63	0.50
S. HEALTHCARE	1112.1**	28	2185.8	29	98.0	5	179.6	-4	8.8	10.7	36.9	22	2.41
IVERSAL HEALTH SERVICES	287.0**	34	558.6	28	12.2	28	27.7	30	4.3	4.5	14.4	16	1.46
VCOR	634.6	10	1260.9	12	30.9	46	58.5	38	4.9	3.6	3.0	77	0.34
MEDICAL PRODUCTS													
GROUP COMPOSITE	13630.9	9	26957.9	10	1732.3	10	3487.2	18	12.7	12.6	23.7	25	1.87
BOTT LABORATORIES	2699.2	8	5371.4	7	470.4	11	950.5	13	17.4	17.0	39.4	19	2.28
RD (C. R.)	295.2	1	584.4	3	27.5	10	54.6	9	9.3	8.6	15.9	19	1.61
JSCH & LOMB	545.6	2	1014.8	1	30.3	41	52.8	-27	5.5	9.6	10.1	24	1.62
KTER INTERNATIONAL	1335.0	5	2634.0	8	142.0	25	280.0	32	10.6	8.9	11.8	28	1.61
STON, DICKINSON (3)	692.9	-2	1398.7	0	77.2	16	152.0	15	11.1	9.5	21.4	18	4.16
STON SCIENTIFIC	357.2	29	679.6	26	23.5	-52	22.5	NM	6.6	17.6	5.8	NM	0.26
IDANT	265.5	18	517.6	15	-46.2	NM	-17.7	NM	NM	9.5	11.9	97	0.57
INSON & JOHNSON	5382.0	13	10716.0	16	791.0	20	1581.0	20	14.7	13.9	27.2	24	2.03
TRONIC (8)	596.1	15	1125.3	21	125.4	43	234.4	47	21.0	17.0	26.4	27	1.88
ENS & MINOR	749.9	1	1521.3	2	2.9	74	4.5	-29	0.4	0.2	-14.9	NM	-0.59
JUDE MEDICAL	203.2	4	402.2	5	36.6	3	75.0	10	18.0	18.3	17.0	19	1.84
RYKER	225.4	-1	443.0	0	24.5	20	49.5	20	10.9	8.9	20.0	25	0.99
S. SURGICAL	283.6	8	549.6	9	27.2	42	48.1	44	9.6	7.2	7.9	23	1.29
HOUSING & REAL ESTATE													
GROUP COMPOSITE	13345.7	13	24430.7	11	224.0	-70	370.4	-68	1.7	6.3	12.6	24	1.33
BUILDING MATERIALS													
GROUP COMPOSITE	9822.8	10	18136.3	9	184.9	-71	268.8	-73	1.9	7.2	15.3	25	1.43
ERICAN STANDARD	1519.0	11	2883.3	11	61.0	23	-142.2	NM	4.0	3.6	NM	NM	-0.98
FARGE	420.9	6	624.7	5	43.3	-13	5.1	-34	10.3	12.6	13.5	10	1.83
RTIN MARIETTA MATERIALS	200.5	14	337.0	10	26.8	34	31.1	10	13.4	11.3	15.9	15	1.54
RTEK	260.2	34	481.2	27	5.8	81	8.2	44	2.2	1.6	14.0	8	1.47
ENS CORNING	956.0	9	1805.0	5	-473.0	NM	-434.0	NM	NM	7.2	NM	NM	-5.81
Y GEM INDUSTRIES	212.1	4	354.1	-3	4.2	304	1.5	NM	2.0	0.5	-3.0	NM	-0.29
G INDUSTRIES	1913.6	2	3662.4	1	228.5	5	400.8	-8	11.9	11.6	29.5	12	3.78
M (7)	316.9	12	572.0	11	24.6	20	32.7	16	7.8	7.2	15.5	17	0.90
ERWIN-WILLIAMS	1145.3	27	2003.0	24	81.9	12	101.5	10	7.2	8.1	17.2	18	2.44
CUMSEH PRODUCTS	490.9	5	987.1	5	33.9	-4	64.9	-8	6.9	7.6	12.3	10	5.21
AS INDUSTRIES (7)	256.0**	12	491.1	15	25.4	38	41.4	64	9.9	8.0	20.2	9	7.05
Q	642.0	4	1244.0	3	4.0	NM	-11.0	NM	0.6	NM	NM	NM	-0.82
LSPAR (2)	208.5	2	373.8	2	14.1	16	20.4	16	6.8	5.9	22.4	20	2.28
LCAN MATERIALS	419.2	10	727.8	7	58.6	23	78.7	24	14.0	12.5	22.8	11	5.09
RK INTERNATIONAL	861.7	11	1589.8	15	45.9	29	69.8	29	5.3	4.6	-11.5	NM	-1.92
CONSTRUCTION & REAL ESTATE													
GROUP COMPOSITE	3522.9	23	6294.4	20	39.1	-59	101.6	-37	1.1	3.3	7.2	19	1.02
PSTEAD MORTGAGE	204.1	15	403.2	15	32.2	81	59.0	78	15.8	10.0	20.7	11	2.65
AMPION ENTERPRISES	256.6	24	449.6	19	11.8	35	19.6	35	4.6	4.2	27.8	18	1.14
INTINENTAL HOMES HOLDING (7)	175.0**	54	316.2	38	9.1	189	15.2	145	5.2	2.8	20.5	5	3.71
UFMAN & BROAD HOME (1)	482.4	53	784.8	44	-98.5	NM	-94.4	NM	NM	1.2	-19.3	NM	-1.75
NNAR (1)	258.3**	23	484.8	24	18.3	-7	35.5	2	7.1	9.3	11.1	12	1.97
D.C. HOLDINGS	237.8**	11	437.0	8	4.5	5	8.9	5	1.9	2.0	8.5	7	0.90
KWOOD HOMES (3)	264.1**	17	485.3	17	17.9	46	34.0	54	6.8	5.4	18.0	16	1.36
ILTE	588.4**	21	1020.9	25	16.4	73	21.5	137	2.8	2.0	8.6	11	2.27
LAND GROUP	414.3	6	741.7	1	5.4	NM	6.4	NM	1.3	NM	-6.2	NM	-1.20
S. HOME	293.2**	13	566.0	8	10.1	29	19.4	21	3.4	3.0	12.6	6	3.36
EBB (DEL) (6)	348.9**	30	605.0	30	11.9	25	-23.4	NM	3.4	3.6	-2.7	NM	-0.44

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE-EARNINGS RATIO 7-19	1 MO. EARN. P. SH.
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
14 LEISURE TIME INDUSTRIES													
INDUSTRY COMPOSITE	26638.4	16	50317.9	15	2163.6	20	3339.8	6	8.1	7.9	13.6	23	1.7
(A) EATING PLACES													
GROUP COMPOSITE	4940.2	7	9600.5	8	498.8	12	873.8	16	10.1	9.7	16.8	22	1.5
BOB EVANS FARMS (8)	198.3	5	393.1	5	-5.8	NM	1.8	-93	NM	6.5	7.0	20	0.9
CRACKER BARREL OLD COUNTRY STORE (5)	220.6	17	440.1	17	16.3	8	28.8	5	7.4	8.0	12.6	19	1.1
DARDEN RESTAURANTS (7)	829.5	-1	1624.6	-1	34.5	91	70.1	NM	4.2	2.2	6.3	19	0.9
FOODMAKER (3)	243.1**	0	493.1	4	5.5	110	9.5	NM	2.3	1.1	45.2	16	0.4
HOTEL MARRIOTT SERVICES	290.3	12	550.1	12	3.3	NM	-1.6	NM	1.1	NM	NA	NA	0.6
MCDONALD'S	2665.1	8	5091.1	10	420.4	11	722.0	9	15.8	15.4	18.6	22	2.0
OUTBACK STEAKHOUSE	236.5	29	452.6	31	18.2	27	35.1	30	7.7	7.9	23.4	19	1.3
SHONEY'S (2)	256.8	1	555.9	-1	6.4	4	8.1	-43	2.5	2.4	NM	78	0.1
(B) ENTERTAINMENT													
GROUP COMPOSITE	5325.1	83	9951.0	68	405.9	28	372.0	-40	7.6	11.5	7.1	30	1.9
DISNEY (WALT) (3)	5087.0	83	9630.0	68	406.0	28	382.0	-40	8.0	11.5	7.2	29	1.9
TRUMP HOTELS & CASINO RESORTS	238.1	NA	321.0	NA	-0.1	NA	-10.0	NA	NM	NA	-29.7	NM	-0.3
(C) HOTEL & MOTEL													
GROUP COMPOSITE	6318.3	10	12056.4	10	382.4	34	678.0	36	6.1	5.0	12.9	26	1.4
AZTAR	189.5	30	369.7	32	0.0	-92	0.8	-67	0.0	0.4	-2.0	NM	-0.1
BALLY ENTERTAINMENT	297.6**	21	584.3	23	17.4	88	26.6	98	5.9	3.8	32.9	20	1.3
CIRCUS CIRCUS ENTERPRISES (11)†	352.9**	20	676.5	18	43.5	10	79.1	13	12.3	13.4	10.8	24	1.3
HARRAH'S ENTERTAINMENT	401.2	3	784.3	5	30.0	-15	61.4	4	7.5	9.1	11.8	29	0.7
HILTON HOTELS	470.0**	11	899.9	12	59.2	12	95.8	13	12.6	12.5	14.7	28	3.7
ITT	1752.0	5	3140.0	4	96.0	43	116.0	59	5.5	4.0	7.1	33	1.1
MARRIOTT INTERNATIONAL	2352.0	11	4515.0	9	75.0	27	138.0	14	3.2	2.8	23.6	25	2.0
MGM GRAND	190.5	13	399.8	21	20.6	NM	55.2	NM	10.8	NM	15.8	20	2.1
MIRAGE RESORTS	312.7	5	686.9	5	40.6	42	105.2	31	13.0	9.6	16.1	21	1.0
(D) OTHER LEISURE													
GROUP COMPOSITE	10054.7	6	18710.0	6	876.5	17	1416.1	12	8.7	7.9	18.5	20	1.9
AMERICAN GREETINGS (10)	438.2	0	984.0	5	27.8	-26	73.1	-9	6.3	8.5	8.4	17	1.4
BRUNSWICK	891.7	6	1657.5	3	70.8	91	116.2	50	7.9	4.4	16.0	11	1.7
CALLAWAY GOLF	210.0	35	345.1	26	38.9	42	58.4	32	18.5	17.6	38.0	20	1.6
CARNIVAL (1)	516.8	14	965.6	11	106.3	18	183.4	17	20.6	19.8	19.9	17	1.6
EASTMAN KODAK	4117.0	5	7505.0	6	440.0	17	714.0	12	10.7	9.6	27.9	19	3.8
FLEETWOOD ENTERPRISES (8)	772.0	9	1397.5	3	12.7	-7	27.7	-7	1.6	1.9	10.8	20	1.5
HARLEY-DAVIDSON	392.8**	10	763.9	17	39.9	20	72.9	28	10.2	9.3	22.1	25	1.6
HASBRO	511.6	6	1050.3	4	6.0	NM	30.4	347	1.2	NM	11.5	17	2.0
HUFFY	199.6	0	386.1	-4	4.6	NM	7.5	58	2.3	0.2	-6.3	NM	-0.5
MATTEL	777.4	2	1363.2	4	66.3	-2	96.2	2	8.5	8.8	27.6	20	1.2
OUTBOARD MARINE (3)	291.0	-12	576.5	11	-3.6	NM	-2.5	NM	NM	8.5	-2.7	NM	-0.3
POLAROID	581.6	2	1042.7	6	28.5	24	-32.2	NM	4.9	4.0	-18.8	NM	-2.6
ROYAL CARIBBEAN CRUISES	355.0	26	672.6	21	38.3	21	71.0	-14	10.8	11.2	14.2	11	2.1
15 MANUFACTURING													
INDUSTRY COMPOSITE	39617.3	11	75238.7	11	2643.0	45	4717.9	32	6.7	5.1	19.6	15	2.2
(A) GENERAL MANUFACTURING													
GROUP COMPOSITE	11880.7	15	22563.7	13	806.5	184	1375.5	69	6.8	2.8	17.3	20	1.7
AVERY DENNISON	797.7	2	1594.3	3	41.6	17	81.6	16	5.2	4.6	19.0	18	2.9
CARLISLE	262.3	31	487.4	25	16.4	32	27.0	29	6.3	6.2	18.4	16	3.2
CORNING	913.7**	19	1751.3	25	93.8	NM	156.4	NM	10.3	NM	15.1	26	1.4
DURACELL INTERNATIONAL (6)	562.3	15	966.6	13	51.4	11	70.8	1	9.1	9.5	17.4	20	2.0
FEDERAL SIGNAL	232.3	17	443.1	15	16.0	10	27.8	10	6.9	7.3	20.8	19	1.1
FOAMEX INTERNATIONAL	322.5	9	616.3	2	8.4	98	14.5	48	2.6	1.4	NM	NM	-1.8
GRIFFON (3)	180.5	33	330.9	30	8.0	58	11.9	43	4.4	3.7	16.0	10	0.7
HARSCO†	387.7	3	754.4	3	29.3	19	60.4	21	7.5	6.5	16.5	15	4.2
HILLENBRAND INDUSTRIES (1)	424.2	5	848.1	7	33.6	21	67.0	21	7.9	6.9	14.4	24	1.4
ILLINOIS TOOL WORKS	1324.8	21	2461.7	11	130.4	33	229.1	26	9.8	9.7	20.1	18	3.6
INTERNATIONAL GAME TECHNOLOGY (3)	196.6	30	357.2	19	34.7	37	54.1	12	17.7	16.8	17.1	23	0.7
JOHNSON CONTROLS (3)	2705.6	14	5146.0	22	69.3	25	105.7	21	2.6	2.5	16.0	13	5.0
MARK IV INDUSTRIES (10)	616.9	19	1151.9	15	28.5	16	49.2	17	4.6	4.7	13.3	14	1.5
NEWELL	735.1	18	1353.3	15	67.7	23	100.9	11	9.2	8.8	17.8	20	1.4
POLARIS INDUSTRIES	317.1	11	595.1	10	16.3	30	29.6	16	5.1	4.4	50.2	12	2.3
RUBBERMAID	573.0	3	1106.2	1	44.8	55	86.4	4	7.8	5.2	6.2	66	0.4
SEALED AIR	193.1	6	379.0	7	17.6	39	33.5	38	9.1	6.9	58.3	23	1.4
TELEFLEX	238.4	3	472.8	3	15.1	14	30.0	17	6.4	5.7	14.4	16	2.9
TRINOVA	517.9	3	1030.0	4	33.1	1	57.5	3	6.4	6.6	22.9	9	3.2
UPPERWARE	379.0	2	718.0	4	50.6	6	82.2	5	13.4	13.6	37.1	15	2.7
(B) MACHINE & HAND TOOLS													
GROUP COMPOSITE	4751.5	8	9168.1	8	225.6	17	358.0	-1	4.7	4.4	14.0	17	1.8
BLACK & DECKER	1207.9	6	2272.9	5	45.3	61	12.9	-73	3.8	2.5	13.1	20	1.9
CINCINNATI MILACRON	411.4	-1	764.8	3	14.7	75	27.3	28	3.6	2.0	40.7	6	3.1
SKIDMORE OWINGS & MERRILL	434.9	24	844.5	23	32.5	22	59.5	24	7.5	7.6	17.2	20	1.9

INDUSTRY SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6/30	PRICE-EARNINGS RATIO 7/19	12 MONTHS EARNINGS PER SHARE
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
DUNGS & LEWIS	199.6	17	392.1	20	9.3	0	19.7	20	4.6	5.4	1.9	41	0.28
INAMETAL (6)	279.8	5	565.9	6	18.9	-20	42.2	8	6.7	8.9	16.4	12	2.62
COLN ELECTRIC	284.5	6	563.2	6	20.2	16	36.8	10	7.1	6.5	18.0	12	2.61
CO INDUSTRIES	560.9	8	1120.4	10	14.0	-5	26.9	-2	2.5	2.8	17.1	7	7.24
IP-ON	384.6**	18	728.9	15	34.5	16	64.2	14	9.0	9.1	15.4	15	2.99
	310.6	6	602.9	6	3.5	-1	6.3	67	1.1	1.2	0.7	NM	0.08
NLEY WORKS	677.2	3	1312.5	1	32.6	4	62.2	3	4.8	4.8	8.0	44	0.69
SPECIAL MACHINERY													
GROUP COMPOSITE	19649.1	11	37188.1	11	1463.5	18	2633.7	20	7.4	7.0	23.0	13	3.08
ELIED MATERIALS (2)	1127.9	67	2168.4	84	185.8	98	357.4	124	16.5	13.9	30.8	7	3.57
IE	1398.0	2	2503.0	-1	110.0	0	185.0	3	7.9	8.0	19.1	10	4.71
ERPILLAR	4180.0	-1	8024.0	-1	374.0	16	670.0	8	8.9	7.7	32.5	11	6.07
TEC INDUSTRIES	306.0	2	599.0	2	18.0	7	19.3	-39	5.9	5.6	NM	22	0.62
RE (2)	3088.7**	10	5406.2	10	272.7	15	438.9	17	8.8	8.4	23.0	12	2.93
ER	1023.4	8	2022.9	12	87.9	11	165.6	19	8.6	8.3	23.8	16	2.69
SSER INDUSTRIES (2)	1629.6	29	3092.5	21	57.2	27	103.8	24	3.5	3.6	14.4	22	1.28
	1250.7	12	2345.0	10	57.4	-27	114.2	-15	4.6	7.1	28.3	13	5.13
ERNISCHFEGER INDUSTRIES (2)	741.8	34	1385.4	37	33.6	59	56.7	134	4.5	3.8	20.7	12	2.67
ERSOLL-RAND	1761.8	27	3366.7	31	92.3	39	166.8	48	5.2	4.8	17.6	13	3.04
ITAIR	362.9	7	729.2	9	17.1	28	33.6	24	4.7	3.9	13.0	16	1.64
WART & STEVENSON SERVICES (11)	219.5	-24	520.9	-10	6.7	-58	20.6	-40	3.1	5.5	11.1	14	1.58
KEN	601.6	3	1197.5	4	34.5	11	68.1	4	5.7	5.3	13.1	11	3.67
CO INTERNATIONAL (6)	1372.1	10	2629.7	10	94.2	32	173.7	27	6.9	5.7	16.9	20	2.03
ITY (11)	585.1	-2	1197.7	-2	22.0	-35	59.8	-15	3.8	5.7	13.5	16	2.74
TEXTILES													
GROUP COMPOSITE	3336.0	6	6318.8	3	147.5	38	350.7	76	4.4	3.4	17.1	13	1.27
LINS & AIKMAN (11)	373.6	12	699.7	5	14.8	-40	182.8	256	4.0	7.4	NM	2	3.11
IE MILLS	208.1	-11	407.4	-11	3.7	NM	10.9	294	1.8	NM	1.1	NM	0.07
DCREST CANNON	277.8	2	527.8	0	2.1	NM	1.4	-28	0.8	NM	-9.6	NM	-2.33
LFORD MILLS (3)	232.2	10	439.3	6	12.6	12	18.5	-10	5.4	5.3	10.3	12	1.99
IAWK INDUSTRIES	474.6	11	858.2	6	16.4	192	21.7	119	3.5	1.3	6.0	35	0.52
AW INDUSTRIES	785.7	6	1443.5	2	28.1	50	12.5	-46	3.6	2.5	7.6	32	0.39
INGS INDUSTRIES	545.0	2	1128.5	11	43.0	199	55.3	128	7.9	2.7	13.5	9	5.08
FI (6)	439.0	8	814.5	1	26.7	-22	47.5	-27	6.1	8.5	13.4	24	1.18
METALS & MINING													
GROUP COMPOSITE	19034.9	1	36991.8	0	840.2	-11	1513.7	-38	4.4	5.0	14.3	13	2.21
ALUMINUM													
GROUP COMPOSITE	7322.8	5	14080.3	5	300.4	-28	606.7	-25	4.1	6.0	15.9	12	3.49
IMAX	851.4	18	1654.0	17	83.1	112	178.5	19	9.8	5.4	16.4	5	5.65
MINUM CO. OF AMERICA	3413.1	9	6562.7	7	132.2	-40	310.4	-25	3.9	7.0	15.7	15	3.89
SER ALUMINUM	567.6	-3	1098.7	0	8.2	-65	18.1	-32	1.4	4.0	61.9	19	0.58
XXAM	667.7	-1	1279.9	2	16.9	-33	22.7	-7	2.5	3.8	NM	7	5.90
WOLDS METALS	1823.0	-2	3485.0	-1	60.0	-46	77.0	-60	3.3	6.0	11.3	14	3.64
STEEL													
GROUP COMPOSITE	9220.2	-1	17982.6	-2	293.5	83	385.9	-54	3.2	1.7	12.0	14	1.50
STEEL HOLDING	575.4	-3	1134.3	-6	38.5	-51	75.5	-49	6.7	13.2	26.7	6	6.96
EGHENY LUDLUM	338.6	-13	691.7	-12	20.5	41	39.6	-38	6.0	8.8	25.0	14	1.36
MMERICAL METALS (4)	639.1**	11	1157.3	5	12.0	6	22.0	2	1.9	2.0	13.3	11	2.81
AND STEEL INDUSTRIES	1163.0	-9	2343.9	-7	33.7	-42	50.9	-50	2.9	4.5	10.7	10	1.75
	1075.1	-3	2068.2	-6	32.0	-50	45.3	-61	3.0	5.8	8.7	10	1.14
KENS	256.0	-6	520.1	-2	-5.7	NM	-10.1	NM	NM	3.5	1.0	98	0.22
IONAL STEEL	769.5	4	1451.6	-3	10.4	-66	-5.2	NM	1.4	4.1	2.9	28	0.33
COR	911.1	4	1787.2	4	55.2	-21	107.8	-21	6.1	7.9	17.1	17	2.80
EGON STEEL MILLS	174.1	15	379.5	12	4.1	-28	10.6	39	2.4	3.8	4.5	18	0.76
ANEX (2)	218.3	-7	407.1	-6	8.1	-17	12.2	-16	3.7	4.2	17.3	9	2.25
UGE STEEL	349.0	17	669.2	8	11.8	-53	18.5	-64	3.4	8.5	15.4	8	2.85
X-U. S. STEEL GROUP	1580.0	-3	3171.0	-1	32.0	61	78.0	-50	2.0	5.0	14.9	11	2.47
ALTER INDUSTRIES (7)	398.2	0	727.4	NA	39.7	NM	-78.4	NA	10.0	NM	-28.7	NM	-1.56
IRTON STEEL	335.6	5	676.5	0	-21.6	NM	-24.4	NM	NM	4.0	-7.2	NM	-0.35
IRTHINGTON INDUSTRIES (7)	437.3	8	797.6	3	22.8	-34	43.6	31	5.2	8.5	14.6	19	1.01
OTHER METALS													
GROUP COMPOSITE	2491.9	-7	4928.9	-6	246.3	-33	521.1	-28	9.9	13.8	15.6	14	2.33
PRUS AMAX MINERALS	740.0	-15	1424.0	-15	53.0	-60	115.0	-50	7.2	15.3	-0.5	NM	-0.12
REPORT-McMORAN COPPER & GOLD	424.3	1	812.7	-2	42.7	-21	78.8	-29	10.1	12.9	54.0	36	0.83
ELLER INDUSTRIES	189.6	5	370.1	5	13.9	30	27.2	31	7.3	5.9	16.4	14	2.65
ELPS DODGE	957.7	-7	1962.4	-5	126.3	-21	279.4	-19	13.2	15.6	25.1	6	9.92
OLVERINE TUBE	180.3	10	359.7	5	10.4	17	20.7	15	5.8	5.4	19.8	14	2.44

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-19	MOVS EAR F SH
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
17 NONBANK FINANCIAL													
INDUSTRY COMPOSITE	78441.0	10	152508.2	11	7917.4	32	14884.3	31	10.1	8.4	16.5	12	3.1
(A) FINANCIAL SERVICES													
GROUP COMPOSITE	46069.2	16	88547.5	16	4974.9	49	9299.1	48	10.8	8.4	20.0	12	3.1
ADVANTA	189.7**	32	377.4	35	45.1	35	86.1	34	23.8	23.2	23.6	14	3.1
ALEX. BROWN	310.2**	54	581.1	65	49.8	117	90.5	130	16.1	11.4	26.9	5	9.1
ALLEGHANY	525.0	26	993.1	22	22.8	33	39.6	120	4.3	4.1	8.1	13	14.1
AMERICAN EXPRESS	4044.0**	2	7926.0	2	452.0	10	848.0	11	11.2	10.3	21.0	12	3.1
ASSOCIATES FIRST CAPITAL	1717.0	13	3362.0	14	200.2	23	392.5	19	11.7	10.7	14.3	NA	
AT&T CAPITAL	460.6	21	899.9	21	37.8	35	74.8	41	8.2	7.3	12.7	14	3.1
BENEFICIAL	484.2**	22	1026.3	38	82.4	31	189.8	127	17.0	15.9	17.2	12	4.1
BLOCK (H&R) (8)	712.3**	16	NA	NA	185.0	14	NA	NA	26.0	26.3	35.9	23	1.1
CAPITAL ONE FINANCIAL	308.4	29	612.6	34	38.2	29	76.2	39	12.4	12.4	22.3	13	2.1
COUNTRYWIDE CREDIT INDUSTRIES (10)	292.1	24	600.1	3	60.6	68	118.3	113	20.8	9.4	16.0	11	2.1
DEAN WITTER, DISCOVER	1540.0**	8	3087.5	11	238.8	1	484.6	5	15.5	16.7	17.9	10	5.1
DONALDSON, LUFKIN & JENRETTE	991.2	43	1767.1	39	97.0	131	162.1	104	9.8	6.1	19.3	7	4.1
EDWARDS (A. G.) (10)	428.5	32	833.7	35	56.4	60	105.4	56	13.2	10.9	17.6	9	2.1
EQUIFAX	445.6	9	868.6	10	41.1	15	78.0	19	9.2	8.8	44.9	24	1.1
FANNIE MAE	6146.0**	13	12210.8	14	675.5	17	1350.4	18	11.0	10.6	21.4	15	2.1
FEDERAL HOME LOAN MORTGAGE	2965.0	29	5697.0	29	324.0	23	625.0	20	10.9	11.5	19.3	13	6.1
FIRST AMERICAN FINANCIAL	413.4**	41	760.8	37	19.4	NM	28.0	NM	4.7	0.4	15.6	7	4.1
GREEN TREE FINANCIAL	196.1	28	364.2	29	75.4	22	141.8	26	38.5	40.3	27.9	16	2.1
HOUSEHOLD INTERNATIONAL	1293.5	4	2468.7	-5	124.6	17	235.1	16	9.6	7.9	17.2	15	4.1
LEHMAN BROTHERS HOLDINGS (1)	833.0**	14	1654.0	15	108.0	86	212.0	106	13.0	7.9	10.2	8	2.1
MARSH & McLENNAN	1036.8	11	2107.5	11	115.2	13	258.3	14	11.1	10.9	24.5	15	5.1
MERRILL LYNCH	6190.0**	11	12209.0	13	434.0	53	843.0	65	7.0	5.1	24.4	8	7.1
MONEY STORE	178.4	58	333.1	63	18.9	76	33.1	84	10.6	9.6	16.1	18	1.1
MORGAN STANLEY GROUP (1)	3393.0**	27	6701.0	29	301.0	81	574.0	169	8.9	6.2	20.4	8	5.1
PAINEWEBBER GROUP	1431.2**	7	2861.2	12	92.2	NM	192.7	NM	6.4	NM	20.5	7	3.1
RAYMOND JAMES FINANCIAL (3)	198.2**	33	376.9	37	18.6	34	33.9	42	9.4	9.3	21.8	7	2.1
SALLIE MAE	868.8	11	1762.1	10	103.0	17	205.9	-33	11.9	9.0	49.3	11	6.1
SALOMON	2362.0**	21	4830.0	20	291.0	NM	567.0	NM	12.3	NM	23.0	5	8.1
SCHWAB (CHARLES)	491.8**	44	938.6	47	70.1	58	117.0	41	14.3	13.0	32.7	21	1.1
TRAVELERS GROUP	5426.0	30	9941.0	22	576.0	53	1096.0	61	10.6	9.0	18.5	10	4.1
UNITED ASSET MANAGEMENT	197.3	15	396.2	23	20.8	24	40.0	24	10.5	9.8	14.6	19	1.1
(B) INSURANCE													
GROUP COMPOSITE	29464.3	4	58095.5	5	2657.3	9	5030.0	7	9.0	8.6	13.1	13	4.1
AETNA	3157.1	-3	6467.5	0	24.3	-80	189.8	-11	0.8	3.7	12.4	16	3.1
AFLAC	1741.7	10	3471.6	-5	85.7	-8	172.3	-3	4.9	4.8	16.5	13	2.1
ALLSTATE	6324.0	12	12227.0	9	764.0	47	1188.0	12	12.1	9.2	16.6	9	4.1
AMERICAN GENERAL	1721.0	6	3432.0	9	168.0	-7	337.0	-5	9.8	11.1	9.7	14	2.1
AMERICAN INTERNATIONAL GROUP	6418.6**	8	12492.8	8	724.4	14	1395.6	16	11.3	10.6	13.5	16	5.1
AMERICAN NATIONAL INSURANCE	379.5	7	755.6	7	46.2	19	89.0	6	12.2	11.0	8.9	8	7.1
CINCINNATI FINANCIAL	442.0	9	893.8	9	54.4	-1	113.8	-4	12.3	13.6	8.4	15	3.1
COMMERCE GROUP	186.4	11	366.3	9	16.3	-44	30.9	-40	8.7	17.5	16.5	9	2.1
FREMONT GENERAL	199.7	21	463.3	-11	22.4	33	40.9	32	11.2	6.7	15.6	7	2.1
HORACE MANN EDUCATORS	187.0	1	373.6	2	17.0	5	32.5	-3	9.1	8.8	15.5	10	3.1
LINCOLN NATIONAL	1643.9	0	3284.4	5	111.4	5	251.5	1	6.8	7.2	11.4	9	4.1
MGIC INVESTMENT	183.6	22	359.1	23	62.7	25	121.1	27	34.1	33.3	20.2	16	3.1
PROGRESSIVE	784.5**	16	1516.5	17	78.5	29	141.8	17	10.0	9.0	18.4	14	3.1
SAFECO	1028.9**	4	2011.9	1	106.0	3	216.7	29	10.3	10.3	11.9	9	3.1
SUNAMERICA (3)	399.8**	46	744.3	41	69.7	44	137.9	44	17.4	17.6	19.9	15	3.1
TIG HOLDINGS	462.0**	-3	918.0	-4	34.0	3	3.0	-94	7.4	7.0	6.2	25	1.1
TRANSAMERICA	1515.0	-4	3008.7	0	106.0	-10	221.3	3	7.0	7.5	13.1	10	6.1
UNITRINT	382.1	2	762.7	7	29.5	-29	54.9	-25	7.7	11.1	8.7	13	3.1
UNUM	989.3	-14	1991.9	-6	73.9	-17	146.0	-4	7.5	7.7	12.2	16	3.1
USF&G	858.0	0	1725.0	3	67.0	46	124.0	31	7.8	5.4	13.2	9	1.1
USLIFE	460.2	4	895.6	4	-4.1	NM	22.1	-56	NM	5.9	6.5	14	2.1
(C) SAVINGS & LOAN													
GROUP COMPOSITE	2907.6	0	5865.2	4	285.2	29	555.2	44	9.8	7.6	12.8	10	3.1
AHMANSON (H. F.)	923.2**	-8	1878.6	-3	68.7	7	133.5	14	7.4	6.4	14.1	7	3.1
GOLDEN WEST FINANCIAL	646.3**	5	1302.2	11	76.5	43	152.0	45	11.8	8.7	12.1	11	4.1
GREAT WESTERN FINANCIAL	885.0**	0	1785.9	4	79.3	57	150.6	60	9.0	5.7	10.4	11	2.1
STANDARD FEDERAL BANCORPORATION	269.0**	12	529.7	13	34.0	19	66.2	15	12.7	11.9	13.6	10	3.1
TCF FINANCIAL	184.0**	4	368.7	6	26.7	14	52.9	350	14.5	13.2	19.0	12	2.1

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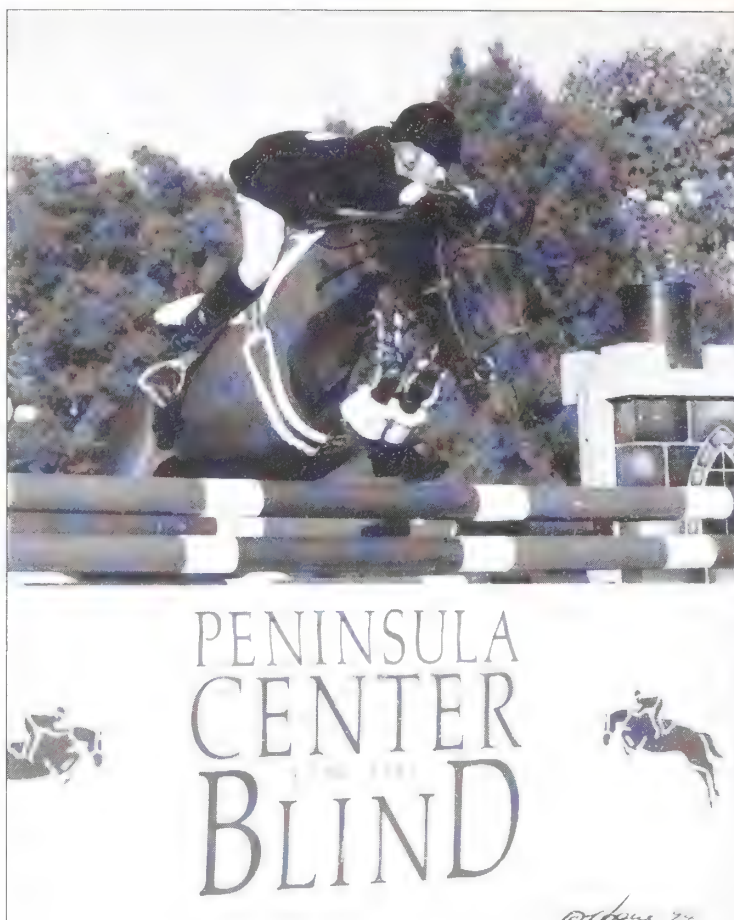
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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-19	12 MONTHS' EARNINGS PER SHARE	
	2ND QUARTER 1996 \$ MIL.	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL.	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL.	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL.	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %				
N INDUSTRIES														
ELLIGENT ELECTRONICS (11)	877.9	6	1812.8	10	-3.2	NM	-8.1	NM	NM	0.6	-15.8	NM	-0.82	
ROAGE (2)	863.6	16	1644.0	16	2.9	21	4.5	-15	0.3	0.3	-0.3	NM	-0.04	
LER (HERMAN) (7)	341.5	17	654.5	19	17.1	NM	29.0	NM	5.0	NM	14.7	18	1.83	
NEY BOWES														
YNOLDS & REYNOLDS (3)	287.0	24	544.1	18	24.3	22	47.3	21	8.5	8.6	25.4	22	2.09	
ANDARD REGISTER	239.4	8	469.0	10	16.1	34	29.6	30	6.7	5.4	12.8	14	1.90	
CH DATA (11)	985.6	56	1886.6	46	10.4	464	19.6	157	1.1	0.3	10.0	24	0.78	
LLACE COMPUTER SERVICES (5)	213.8	19	433.3	22	17.5	21	37.0	33	8.2	8.0	13.9	19	3.06	
COMPUTERS & PERIPHERALS														
ROUP COMPOSITE	54235.1	11	105757.0	12	2758.7	-25	4853.7	-27	5.1	7.5	13.6	20	2.06	
PLE COMPUTER (3)	2179.0	-15	4364.0	-17	-32.0	NM	-772.0	NM	NM	4.0	-38.0	NM	-6.33	
MPAQ COMPUTER	4001.0	14	8206.0	27	267.0	9	501.0	8	6.7	7.0	16.0	16	3.00	
IL COMPUTER (11)	1638.0	44	3176.8	46	82.0	33	151.8	24	5.0	5.4	37.2	16	2.95	
ITAL EQUIPMENT (6)	3719.3	-1	7340.3	2	-432.8	NM	-308.8	NM	NM	4.3	-4.1	NM	-0.97	
C														
TEWAY 2000	545.0	14	1066.5	15	87.1	-8	171.6	-4	16.0	19.7	26.1	14	1.28	
WLETT-PACKARD (2)	1137.3	48	2279.5	48	51.4	48	101.8	39	4.5	4.5	36.3	14	2.57	
ERNATIONAL BUSINESS MACHINES	9880.0	33	19168.0	30	723.0	25	1513.0	28	7.3	7.8	21.3	16	2.63	
18183.0	4	34742.0	4	1347.0	-22	2556.0	-15	7.4	9.8	15.2	15	6.06		
EGA														
MARK INTERNATIONAL GROUP	555.3	3	1143.1	13	30.8	55	52.4	67	5.5	3.7	16.6	17	0.92	
CRON ELECTRONICS (4)	412.3	52	868.9	88	14.1	-10	1.5	-95	3.4	5.7	19.9	25	0.43	
AGATE TECHNOLOGY (6)	2014.5	-3	4107.9	4	101.0	-10	-56.5	NM	5.0	5.5	9.2	20	2.06	
N MICROSYSTEMS (6)														
NDEM COMPUTERS (3)	465.8	-7	1042.0	3	23.3	-17	-26.2	NM	5.0	5.6	-2.4	NM	-0.22	
OM (7)	660.3	39	1266.3	40	29.5	-46	104.1	1	4.5	11.4	19.7	38	1.01	
ISYS														
STERN DIGITAL (6)	820.7	40	1549.1	39	32.7	24	52.2	13	4.0	4.5	21.3	12	2.01	
ROX	4217.0	4	8145.0	4	293.0	15	530.0	20	6.9	6.3	31.4	14	3.66	
COMPUTER SOFTWARE & SERVICES														
ROUP COMPOSITE	16822.2	24	32629.4	24	1275.5	-9	3090.8	12	7.6	10.3	17.0	44	1.14	
OBE SYSTEMS (1)	204.3	8	398.0	5	34.1	-3	67.7	-5	16.7	18.6	12.2	28	1.19	
ERICAN MANAGEMENT SYSTEMS	188.8	20	370.2	26	8.3	26	14.9	30	4.4	4.2	17.7	34	0.80	
Y NETWORKS (6)	535.5	31	1057.3	39	55.1	-1	84.3	-11	10.3	13.7	18.8	22	1.04	
M INTERNATIONAL	251.9	18	477.0	18	6.7	72	12.1	67	2.6	1.8	15.0	30	1.69	
BLETRON SYSTEMS (10)														
DENCE DESIGN SYSTEMS	177.0	38	340.5	39	28.6	68	54.2	77	16.2	13.2	87.3	20	1.32	
RIDIAN	361.5	10	730.5	12	40.8	39	88.2	36	11.3	9.0	54.0	33	1.51	
SCO SYSTEMS (5)	985.1	93	1811.6	88	229.7	84	426.0	139	23.3	24.5	33.6	41	1.28	
MDISCO (3)														
MPUSERVE (8)	215.2	31	NA	NA	-1.1	NM	NA	NA	NM	NM	19.3	21	0.66	
MPUTER ASSOCIATES INTERNATIONAL (9)	792.0	37	1902.4	38	119.8	35	384.9	28	15.1	15.3	-1.7	NM	-0.09	
MPUTER SCIENCES (9)	1165.1	21	2325.6	17	33.2	20	80.9	21	2.9	2.9	11.3	27	2.57	
LECTRONIC DATA SYSTEMS														
ST DATA	1200.4	18	2330.1	22	139.8	40	245.6	34	11.6	9.8	-0.7	NM	-0.17	
SERV	196.5	13	391.2	18	15.2	27	29.9	29	7.7	6.9	-11.8	NM	-1.16	
ECH HOLDINGS (10)	211.2	18	403.8	11	18.2	-1	34.1	32	8.6	10.2	21.1	19	1.54	
FORMIX														
TERGRAPH	268.2	3	524.9	1	-15.2	NM	-21.6	NM	NM	NM	-4.7	NM	-0.48	
CROSOFT (6)	2255.0	39	4460.0	39	559.0	52	1121.0	47	24.8	22.7	31.8	35	3.43	
IVELL (2)	188.2	-64	626.1	-39	-55.4	NM	8.2	-95	NM	18.1	10.6	24	0.45	
ACLE (7)														
EGUARD SCIENTIFICS	527.4	42	957.5	34	5.4	13	9.4	13	1.0	1.3	13.3	55	1.17	
BASE	249.9	4	493.6	8	-24.6	NM	-31.5	NM	NM	NM	-5.6	NM	-0.32	
NSTAR (8)	485.7	23	932.5	25	16.5	NM	-0.2	NM	3.4	0.2	6.3	65	0.23	
ANG LABORATORIES (6)	268.1	-6	533.1	-1	8.2	44	13.2	NM	3.1	2.0	-11.5	NM	-0.64	
PAPER & FOREST PRODUCTS														
INDUSTRY COMPOSITE	25240.7	-6	49135.3	-4	996.5	-50	2261.9	-36	3.9	7.5	12.6	16	2.75	
FOREST PRODUCTS														
ROUP COMPOSITE	6670.0	-8	12850.4	-8	85.9	-85	265.3	-74	1.3	7.8	12.7	13	3.33	
ISE CASCADE	1261.5	-1	2489.1	0	-17.0	NM	8.6	-95	NM	8.3	12.2	11	2.95	
ORGIA-PACIFIC	3319.0	-10	6368.0	-11	10.0	-96	60.0	-88	0.3	7.2	16.4	12	6.40	
UISIANA-PACIFIC	658.3	-7	1242.4	-11	21.0	-20	17.4	-78	3.2	3.7	-6.9	NM	-1.07	
YONIER														
IVERSAL FOREST PRODUCTS	275.7	17	435.3	6	8.2	55	10.8	23	3.0	2.3	17.1	13	0.91	
ILLAMETTE INDUSTRIES	858.8	-14	1724.9	-9	48.3	-64	121.6	-48	5.6	13.4	21.2	8	7.30	
PAPER														
ROUP COMPOSITE	18570.6	-5	36284.9	-3	910.6	-37	1996.6	-20	4.9	7.4	12.5	16	2.61	
WATER	454.0	-7	922.8	-1	44.3	-26	157.2	50	9.8	12.3	29.3	5	6.82	
AMPION INTERNATIONAL	1444.6	-18	2977.8	-12	15.6	-92	99.2	-69	1.1	10.7	14.8	7	5.77	
ESAPEAKE	276.6	-12	554.3	-9	3.9	-79	11.8	-70	1.4	5.9	14.1	9	2.74	
NSOLIDATED PAPERS														
JRT HOWARD	402.4	-2	788.1	1	36.4	377	63.3	NM	9.0	1.8	NM	13	1.52	
INTERNATIONAL PAPER	5100.0	0	9900.0	3	99.0	-69	197.0	-65	1.9	6.2	8.4	13	2.97	

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE-EARNINGS RATIO 7-19	MO'S EARN'G PER SHARE
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
JAMES RIVER CORP. OF VIRGINIA	1496.8	-18	2983.4	-14	30.5	-26	51.0	-24	2.0	2.3	3.5	43	0
KIMBERLY-CLARK	3347.7	-1	6549.8	0	364.7	19	679.5	34	10.9	9.1	5.2	NM	0
MEAD	1258.5	13	2325.7	-13	67.1	-34	98.0	-40	5.3	7.1	12.6	10	5
POTLATCH	386.1	-3	774.7	-2	18.1	-24	23.1	-51	4.7	6.0	8.8	13	2
SCHULLER	381.4	8	707.5	4	28.2	44	156.5	291	7.4	5.5	43.8	8	1
WESTVACO (2)	760.3	-6	1509.0	-2	50.6	-22	112.9	-1	6.7	8.1	13.1	11	2
WEYERHAEUSER	2886.3	-4	5491.5	4	103.2	58	245.2	-46	3.6	8.2	13.1	15	2

20 PUBLISHING & BROADCASTING

INDUSTRY COMPOSITE	10860.7	10	20774.4	10	557.2	-16	878.5	-18	5.1	6.7	6.0	57	0
BELO (A. H.)	212.8	12	400.1	13	25.5	20	38.2	17	12.0	11.2	11.5	21	1
DOW JONES	630.6	9	1215.5	8	52.0	5	89.7	-6	8.3	8.5	10.8	20	1
DUN & BRADSTREET	1377.9	5	2649.9	5	-25.4	NM	62.3	-76	NM	11.2	10.9	78	0
GANNETT	1208.7	19	2312.8	20	150.0	8	239.4	6	12.4	13.8	22.4	19	3
HOUGHTON MIFFLIN	178.2	70	241.0	55	9.5	NM	-12.6	NM	5.3	NM	1.8	NM	0
K-III COMMUNICATIONS	335.6	30	650.6	31	-14.6	NM	-35.4	NM	NM	NM	-48.5	NM	-0
KNIGHT-RIDDER	717.0	4	1414.6	4	42.4	-55	65.9	-49	5.9	13.7	9.2	32	2
McGRAW-HILL	710.9	0	1294.8	1	57.2	8	73.4	10	8.0	7.4	22.6	17	2
MEDIA GENERAL	192.6	11	377.4	11	20.9	58	35.9	39	10.8	7.6	16.8	15	2
NEW YORK TIMES	645.2	6	1267.7	7	46.8	8	79.5	13	7.3	7.1	9.0	20	1
SCHOLASTIC (7)	282.7	24	498.8	22	1.7	-88	10.6	-53	0.6	6.3	11.6	34	1
SCRIPPS (E. W.)	277.3	7	531.6	5	29.1	7	48.8	4	10.5	10.5	8.0	36	1
TIME WARNER†	2139.0	12	4207.0	13	-31.0	NM	-124.0	NM	NM	NM	-7.9	NM	-0
TIMES-MIRROR	837.3	-1	1644.1	2	46.0	58	72.1	58	5.5	3.5	-34.8	NM	-3
TRIBUNE	641.9	11	1179.0	7	84.3	15	134.7	-1	13.1	12.7	17.4	18	3
WASHINGTON POST	471.9	8	889.5	6	63.2	23	100.2	5	13.4	11.8	16.4	17	17

21 SERVICE INDUSTRIES

INDUSTRY COMPOSITE	28720.9	14	56215.4	14	1218.5	6	1970.8	-8	4.2	4.6	13.8	23	1
(A) CONSTRUCTION & ENGINEERING													
GROUP COMPOSITE	4065.7	11	7997.9	13	102.7	10	194.3	13	2.5	2.6	14.5	20	2
APOGEE ENTERPRISES (10)	228.6	4	443.1	4	5.0	43	8.5	45	2.2	1.6	13.9	22	1
BUTLER MFG.	193.4	-6	369.1	-8	5.8	-6	9.1	-7	3.0	3.0	20.5	10	2
EG&G	355.9	4	702.7	3	14.1	15	26.0	20	4.0	3.6	16.1	16	1
FLUOR (2)	2582.2	16	4984.6	16	63.7	15	121.1	15	2.5	2.5	16.1	21	2
JACOBS ENGINEERING GROUP (3)	436.8	-2	923.8	10	10.4	24	20.3	27	2.4	1.9	15.6	15	1
STONE & WEBSTER	268.7**	16	574.5	27	3.7	-53	9.3	-27	1.4	3.4	3.3	38	0
(B) INDUSTRIAL DISTRIBUTION													
GROUP COMPOSITE	11342.1	21	22478.3	20	395.3	11	871.6	10	3.5	3.8	16.3	16	2
APS HOLDING (11)	217.6	58	368.0	34	1.4	-64	-4.7	NM	0.6	2.7	5.5	44	0
ARROW ELECTRONICS	1601.7	10	3305.0	14	54.1	5	110.9	15	3.4	3.6	16.6	9	4
BOISE CASCADE OFFICE PRODUCTS	460.8	51	922.2	51	13.6	66	29.2	83	3.0	2.7	15.9	26	0
CASTLE (A. M.)	174.8	7	349.8	5	7.0	3	14.6	-3	4.0	4.2	23.0	11	1
CELLSTAR (1)	225.6	27	430.5	17	-3.1	NM	-2.3	NM	NM	2.9	9.2	15	0
CRANE	466.2	27	902.7	2	22.1	10	40.3	21	4.7	4.5	20.5	14	2
ENRON	2960.9	15	6014.9	35	116.7	24	329.5	14	3.9	4.4	16.9	19	2
GENUINE PARTS	1444.9	15	2844.8	10	80.8	8	154.7	7	5.6	5.7	19.1	16	2
GETTY PETROLEUM (11)	204.3	5	398.9	0	-5.2	NM	0.1	NM	NM	0.9	6.3	28	0
GRAINGER (W. W.)	888.6	9	1731.3	7	49.5	25	99.7	15	5.6	4.9	16.4	18	3
HUGHES SUPPLY (11)	315.6	19	577.5	18	4.3	27	8.1	25	1.4	1.3	11.0	13	2
KAMAN	246.5**	11	486.6	13	5.4	16	10.6	4	2.2	2.1	10.2	12	0
MARSHALL INDUSTRIES (7)	305.4	9	593.4	9	12.0	-2	24.2	9	3.9	4.3	15.2	9	2
PIONEER-STANDARD ELECTRONICS (9)	375.2	67	756.9	62	6.2	10	13.8	-2	1.6	3.0	15.7	12	1
REXEL	291.9	1	556.6	-2	7.6	53	13.2	44	2.6	1.7	14.0	14	0
UNIVAR (10)	576.4	4	1050.4	5	8.6	11	2.5	-70	1.5	1.4	3.8	63	0
VWR SCIENTIFIC PRODUCTS	279.0	93	555.4	91	3.1	327	5.2	305	1.1	0.5	3.5	58	0
WYLE ELECTRONICS	306.9	20	633.4	25	11.1	27	22.1	43	3.6	3.4	20.5	9	3
(C) POLLUTION CONTROL													
GROUP COMPOSITE	4089.5	-2	7880.6	-2	285.1	-11	531.2	4	7.0	7.6	13.1	19	1
BROWNING-FERRIS INDUSTRIES (3)	1471.4	-5	2845.3	-4	62.0	-42	123.0	-38	4.2	6.9	10.9	17	1
WMX TECHNOLOGIES	2618.1	-1	5035.3	-1	223.0	5	408.2	30	8.5	8.1	14.2	20	1
(D) PRINTING & ADVERTISING													
GROUP COMPOSITE	2489.7	7	4860.3	11	111.6	-5	-241.5	NM	4.5	5.1	1.4	NM	0
ADVO (3)	245.7	-4	477.7	-4	4.4	-55	-2.8	NM	1.8	3.8	NM	20	0
DONNELLEY (R. R.) & SONS	1577.5	-6	3124.5	11	54.3	-16	-322.6	NM	3.4	4.3	-7.7	NM	-0
OMNICOM GROUP	666.5	17	1258.1	18	53.0	22	83.9	22	7.9	7.6	28.1	20	2

CORPORATE SCOREBOARD

MPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE EARNINGS RATIO 7-19	12 MONTHS EARNINGS PER SHARE
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
OTHER SERVICES													
GROUP COMPOSITE	6733.9	19	12998.4	18	323.8	22	615.2	29	4.8	4.7	14.5	29	1.19
AMERICA INDUSTRIES (2)	262.1**	12	516.5	11	4.7	19	8.7	19	1.8	1.7	12.7	19	1.95
WARNER SECURITY	454.6	-3	904.6	-3	1.9	217	2.4	243	0.4	0.1	15.3	30	0.32
	357.2	14	708.6	17	9.4	20	17.9	26	2.6	2.5	21.1	17	1.73
TAS (7)	194.4	14	377.4	17	21.5	20	40.0	21	11.1	10.5	17.9	32	1.60
INTERNATIONAL (11)	390.0	20	768.0	27	48.3	34	90.9	32	12.4	11.1	22.0	36	0.93
MOLEMAN (8)	261.0	-14	606.6	-9	-20.5	NM	-19.4	NM	NM	0.2	-8.0	NM	-0.67
	179.7**	87	304.2	78	38.7	92	61.6	91	21.6	21.0	19.5	59	0.93
COM	769.9	46	1411.9	40	4.4	72	7.4	58	0.6	0.5	9.1	15	1.40
ERIM SERVICES	281.2	38	545.9	37	-0.3	NM	5.1	-49	NM	2.7	6.6	32	1.20
APHIS	175.2	24	338.8	23	3.3	-56	16.1	NM	1.9	5.4	3.8	NM	0.27
RELL (2)	240.7	22	461.9	21	6.0	52	11.0	41	2.5	2.0	24.6	30	0.85
(8)	621.3	14	1208.0	16	24.3	17	43.8	17	3.9	3.8	13.9	11	4.65
KERTON'S	200.9	3	401.0	2	3.0	95	4.8	57	1.5	0.8	10.7	14	1.45
STON BRINK'S GROUP	222.1	20	434.6	19	14.0	17	25.9	20	6.3	6.4	19.5	20	1.46
LINS	177.8	1	320.3	1	12.8	-39	19.2	-33	7.2	12.0	13.7	27	0.83
ETY-KLEEN	211.4	4	413.1	4	13.6	12	26.7	10	6.4	6.0	12.7	17	0.96
VICE CORP. INTERNATIONAL	564.7	60	1140.2	62	62.3	53	134.1	52	11.0	11.5	11.3	27	2.01
VICMASTER	916.9	8	1657.2	6	71.3	42	111.8	41	7.8	5.9	26.0	14	1.55
T INFORMATION SCIENCES (2)	252.9**	32	479.5	28	4.9	245	7.2	108	2.0	0.7	18.3	17	2.09
TELECOMMUNICATIONS													
INDUSTRY COMPOSITE	60597.1	7	118699.4	8	6619.6	13	12901.6	15	10.9	10.3	17.1	24	1.73
EQUIPMENT & SERVICES													
GROUP COMPOSITE	29670.5	10	57935.7	11	2566.9	12	4801.2	14	8.7	8.5	5.4	80	0.50
TELECOMMUNICATIONS (2)	193.1	38	355.6	36	19.9	92	36.2	74	10.3	7.4	12.7	40	1.13
TOUCH COMMUNICATIONS†	481.3	19	930.2	20	61.2	58	113.4	53	12.7	9.6	4.5	82	0.33
T	13032.0	2	25988.0	3	1523.0	11	2966.0	12	11.7	10.8	3.0	NM	0.33
ITY TELEPHONE ENTERPRISES†	186.5	19	362.4	19	32.9	26	62.6	18	17.7	16.7	13.5	15	2.09
ASAT	232.3**	10	478.0	14	5.8	-74	15.1	-59	2.5	10.4	1.9	64	0.33
COMMUNICATIONS	356.4	-1	664.3	-2	21.3	-59	32.8	-65	6.0	14.4	11.3	27	1.12
INTERNATIONAL	269.4	77	520.0	76	17.7	59	32.9	53	6.6	7.3	21.9	40	0.73
ENT TECHNOLOGIES	5364.0	6	9941.0	8	72.0	-55	-31.0	NM	1.3	3.1	NM	NM	-1.97
I COMMUNICATIONS	4565.0	23	9056.0	25	305.0	17	600.0	19	6.7	7.0	6.3	26	0.91
INT	3506.4	12	6878.3	11	316.5	30	628.7	34	9.0	7.7	23.9	13	2.87
EPHONE & DATA SYSTEMS†	299.0	29	562.3	27	59.7	164	93.4	104	20.0	9.7	8.4	16	2.51
LABS	189.5	18	361.7	20	-18.7	NM	12.5	-75	NM	17.0	17.6	68	0.86
COMMUNICATIONS†	274.2	31	513.9	32	24.3	NM	31.3	NM	8.9	NM	13.3	78	0.31
CELLULAR†	174.7	49	322.7	49	63.1	162	92.4	94	36.1	20.6	10.2	17	1.69
ROBOTICS (3)	546.8	130	1001.3	131	63.3	155	114.9	478	11.6	10.5	34.1	36	2.03
TELEPHONE COMPANIES													
GROUP COMPOSITE	30926.5	5	60763.7	5	4052.7	14	8100.4	16	13.1	12.0	26.3	16	2.77
TEL	804.5	2	1578.7	2	91.9	-6	176.0	0	11.4	12.5	16.3	15	1.85
ERITECH	3744.0	11	7311.4	12	567.0	13	1045.3	-3	15.1	14.9	26.6	16	3.55
ATLANTIC	3259.5	-9	6467.1	-8	494.3	11	964.8	12	15.2	12.5	28.6	13	4.47
LSOUTH	4620.0	5	9161.0	5	629.0	13	1599.0	45	13.6	12.7	16.1	20	2.07
ICINNATI BELL	376.0	13	738.1	11	44.8	66	86.5	NM	11.9	8.1	18.3	38	1.37
NTIER	670.3	32	1325.4	37	69.2	30	134.3	28	10.3	10.5	17.9	28	1.06
E	5293.0	7	10244.0	7	642.0	11	1258.0	12	12.1	11.8	38.6	15	2.75
NEX	3445.8	-1	6754.8	-1	358.0	49	571.8	16	10.4	6.9	18.2	17	2.66
SIFIC TELESIS GROUP	2393.0	7	4727.0	5	281.0	8	579.0	7	11.7	11.7	47.6	14	2.53
COMMUNICATIONS	3332.7	10	6529.4	10	501.0	13	965.0	15	15.0	14.6	31.3	15	3.31
UTHERN NEW ENGLAND TELECOMMS.	487.8**	9	961.8	8	50.5	26	102.7	18	10.4	9.0	47.9	14	2.83
WEST COMMUNICATIONS GROUP	2500.0	7	4965.0	7	324.0	11	618.0	2	13.0	12.5	32.0	12	2.52
TRANSPORTATION													
INDUSTRY COMPOSITE	42148.0	10	81319.7	9	2580.6	38	3391.4	29	6.1	4.9	14.1	16	2.75
AIRLINES													
GROUP COMPOSITE	20192.8	9	38358.1	9	1383.4	38	1421.0	57	6.9	5.4	34.2	11	3.36
ASKA AIR GROUP	416.7	15	768.1	17	18.0	156	10.8	NM	4.3	1.9	17.6	9	2.71
ERICA WEST AIRLINES	463.9	16	877.1	18	29.5	41	43.2	66	6.4	5.2	10.9	10	1.48
IR	4550.0	6	8858.0	7	293.0	53	450.0	96	6.4	4.5	10.8	16	4.91
NTINENTAL AIRLINES	1639.0	11	3128.0	8	167.0	64	255.0	254	10.2	6.9	102.3	4	6.08
LTA AIR LINES (6)	3360.0	4	6323.0	3	161.0	-35	-114.0	NM	4.8	7.8	4.0	51	1.42
RTHWEST AIRLINES	2540.4	11	4805.2	11	202.8	94	256.2	139	8.0	4.6	NM	8	4.49
UTHWEST AIRLINES	910.3	23	1682.8	24	85.3	43	118.3	65	9.4	8.1	15.6	16	1.51
L	4163.0	9	7898.0	10	226.0	50	233.0	51	5.5	4.0	NM	10	4.86
AIR GROUP	2149.5	8	4017.9	7	200.8	78	168.5	955	9.3	5.7	NM	6	2.86

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-19	MOST EARN- ING STOCK
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
(B) RAILROADS													
GROUP COMPOSITE	9917.3	13	19467.6	13	896.8	54	1561.9	30	9.0	6.6	11.5	19	3
BURLINGTON NORTHERN SANTA FE	2032.0	58	4063.0	54	211.0	70	398.0	77	10.4	9.7	6.6	29	2
CONRAIL	949.0	3	1838.0	1	26.0	-79	57.0	-68	2.7	13.3	4.3	40	1
CSX	2672.0	5	5186.0	4	234.0	NM	380.0	171	8.8	0.7	18.8	12	4
KANSAS CITY SOUTHERN INDUSTRIES†	206.9**	10	408.2	8	22.4	164	42.3	18	10.8	4.5	36.0	7	5
NORFOLK SOUTHERN	1217.3**	2	2378.8	2	199.5	10	367.6	4	16.4	15.2	15.1	15	5
SOUTHERN PACIFIC RAIL	828.1	3	1613.6	3	17.9	NM	24.0	NM	2.2	NM	2.6	NM	0
UNION PACIFIC	2012.0	7	3980.0	13	186.0	24	293.0	5	9.2	8.0	9.8	23	3
(C) TRANSPORTATION SERVICES													
GROUP COMPOSITE	6331.5	10	12275.2	9	228.6	7	326.6	-11	3.6	3.7	11.5	15	2
AIRBORNE FREIGHT	622.4	14	1220.3	13	10.7	373	12.0	190	1.7	0.4	7.7	17	1
AMERICAN FREIGHTWAYS	181.1	28	347.2	27	2.7	-67	3.3	-77	1.5	5.7	1.0	NM	0
FEDERAL EXPRESS (7)	2737.7	11	5273.2	10	115.4	32	142.6	-5	4.2	3.5	12.6	14	5
GATX	337.8**	7	641.4	6	25.7	-14	50.4	-9	7.6	9.4	11.5	11	4
PITTSBURGH BURLINGTON GROUP	363.9	6	716.1	7	8.7	9	12.5	4	2.4	2.3	11.8	11	1
RYDER SYSTEM	1426.0	8	2754.0	8	31.6	-39	41.8	-47	2.2	3.9	9.6	18	1
TRINITY INDUSTRIES (9)	662.5	10	1323.0	6	33.8	23	64.1	20	5.1	4.5	16.1	12	2
(D) TRUCKING & SHIPPING													
GROUP COMPOSITE	5706.4	7	11218.8	5	71.7	0	81.8	-46	1.3	1.3	2.8	53	0
ALEXANDER & BALDWIN	308.0**	14	567.0	10	17.8	402	25.0	163	5.8	1.3	7.4	22	1
APL	641.1**	5	1367.4	-3	20.8	46	24.7	61	3.2	2.1	8.1	18	1
ARKANSAS BEST	414.5	33	815.8	31	-8.8	NM	-18.3	NM	NM	0.5	-37.3	NM	-3
CALIBER SYSTEM	615.9	12	1198.0	9	0.2	NM	9.8	-78	0.0	4.1	8.0	14	1
CONSOLIDATED FREIGHTWAYS	1401.1	6	2723.0	4	13.7	-39	13.9	-70	1.0	1.7	2.4	57	0
HUNT (J. B.) TRANSPORT SERVICES	372.6	13	726.6	14	6.9	NM	9.7	251	1.8	NM	1.3	NM	0
LANDSTAR SYSTEM	329.1	7	624.6	3	7.0	-10	10.2	-19	2.1	2.5	17.1	15	1
ROADWAY EXPRESS	532.7	2	1049.7	1	4.1	NM	6.7	NM	0.8	NM	1.5	83	0
USFREIGHTWAYS	332.1	16	645.8	14	8.1	-17	12.5	-30	2.5	3.4	12.0	16	1
YELLOW	759.3	-2	1501.0	-2	2.0	94	-12.2	NM	0.3	0.1	-11.4	NM	-1
24 UTILITIES & POWER													
INDUSTRY COMPOSITE	43129.6	8	93111.8	12	3546.4	-4	8609.6	2	8.2	9.3	11.7	12	2
(A) ELECTRIC, WATER & COGENERATION													
GROUP COMPOSITE	34732.4	4	72902.9	7	3122.6	-7	7291.3	0	9.0	10.1	12.1	12	2
AES	174.0	4	346.0	2	28.0	6	57.0	11	16.1	15.8	19.4	22	1
ALLEGHENY POWER SYSTEM	550.9	4	1199.0	5	56.1	17	109.9	-15	10.2	9.1	10.6	16	1
AMERICAN ELECTRIC POWER	1401.0	7	2918.8	7	123.6	12	314.6	15	8.8	8.5	13.1	14	3
BALTIMORE GAS & ELECTRIC	731.7	14	1593.0	17	64.6	27	165.3	36	8.8	7.9	11.9	11	2
BOSTON EDISON	389.8	2	777.6	2	27.9	7	53.1	15	7.2	6.9	10.5	11	2
CENTERIOR ENERGY	609.0	0	1214.2	2	33.2	-44	54.0	-52	5.5	9.8	8.5	7	1
CIPSCO	193.8	5	431.7	9	12.9	-7	35.0	28	6.7	7.5	12.1	16	2
CMS ENERGY	936.0	12	2217.0	14	58.0	45	154.0	16	6.2	4.8	14.5	14	2
CONSOLIDATED EDISON CO. OF N. Y.	1539.7	5	3407.1	9	71.4	-7	246.0	-11	4.6	5.2	12.1	9	2
DOMINION RESOURCES	1121.0	8	2360.3	9	105.0	17	266.0	27	9.4	8.6	10.1	14	2
DPL	285.4	6	656.9	4	35.1	1	99.1	3	12.3	12.9	14.0	14	1
DTE ENERGY	871.3	2	1780.9	3	85.5	-7	201.3	-2	9.8	10.7	11.6	11	2
DUKE POWER	1119.7	6	2281.8	5	157.4	14	348.7	3	14.1	13.1	14.0	15	3
EDISON INTERNATIONAL	1813.7	-3	3781.4	3	167.6	-2	346.6	3	9.2	9.2	11.7	9	1
ENOVA	471.0	6	936.9	1	49.0	-2	116.7	0	10.4	11.2	14.7	11	1
FLORIDA PROGRESS	773.6	6	1513.1	5	61.1	6	111.7	5	7.9	7.9	11.7	14	2
FPL GROUP	1474.1	1	2831.8	7	156.7	6	256.9	-1	10.6	10.1	12.7	14	3
GENERAL PUBLIC UTILITIES	912.3	6	1935.2	9	85.1	20	204.7	32	9.3	8.2	15.8	8	4
HAWAIIAN ELECTRIC INDUSTRIES	347.2	9	673.4	8	23.0	12	43.6	8	6.6	6.4	10.9	13	2
KANSAS CITY POWER & LIGHT	226.2	10	432.8	7	27.7	48	52.2	26	12.2	9.1	14.4	13	2
MIDAMERICAN ENERGY	447.9**	21	1004.8	21	30.6	15	84.1	31	6.8	7.2	11.4	12	1
MONTANA POWER	197.9**	-3	462.3	-1	14.3	89	54.6	30	7.2	3.7	6.5	18	1
NEVADA POWER	199.5	1	346.6	9	21.2	58	24.7	38	10.6	7.7	10.5	12	1
NEW ENGLAND ELECTRIC SYSTEM	551.1	3	1137.3	4	37.2	4	100.8	18	6.7	6.7	13.3	10	3
NEW YORK STATE ELECTRIC & GAS	157.4	3	1071.7	6	20.9	15	119.6	19	4.6	5.6	11.2	8	2
NORTHEAST UTILITIES	871.9	4	1900.1	6	20.0	61	93.9	38	2.3	6.0	9.4	7	1
NORTHERN STATES POWER	592.3	0	1311.0	5	43.4	-27	110.6	-14	7.3	10.1	11.9	13	3
OHIO EDISON	599.3	1	1211.0	2	80.4	3	157.7	4	13.4	13.2	12.4	10	2
ORANGE & ROCKLAND UTILITIES	212.4	-13	498.0	-11	6.3	70	20.9	10	3.0	1.5	9.7	13	2
PACIFIC GAS & ELECTRIC	2138.7	-13	4387.4	-8	111.8	-72	372.5	-49	5.2	16.6	10.6	10	2
PACIFICORP	978.6	20	1983.3	19	99.2	6	229.1	10	10.1	11.5	12.7	12	1
PECO ENERGY	989.4	3	2159.9	7	105.5	-33	262.5	-17	10.7	16.5	11.6	10	2
PINNACLE WEST CAPITAL	452.8	15	814.1	10	65.8	40	105.1	37	14.5	12.0	12.1	11	2
PORTLAND GENERAL	233.4	6	534.0	11	34.7	0	85.0	140	14.9	15.8	14.4	11	2
PP&L RESOURCES	669.1	10	1458.3	9	68.3	32	191.6	20	10.2	8.5	13.3	10	2
PUBLIC SERVICE CO. OF COLORADO	484.8	-3	1107.7	-1	34.5	22	99.0	21	7.1	5.7	13.3	12	2

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-19	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 \$ MIL	CHANGE FROM 1995 %	6 MONTHS 1996 \$ MIL	CHANGE FROM 1995 %	2ND QUARTER 1996 %	2ND QUARTER 1995 %			
BLIC SERVICE CO. OF NEW MEXICO	197.6	3	439.5	4	13.5	-42	40.0	-4	6.9	12.2	10.1	11	1.75
BLIC SERVICE ENTERPRISE GROUP	1335.9	5	3133.1	8	129.1	5	326.8	-6	9.7	9.6	12.0	10	2.56
GET SOUND POWER & LIGHT	257.3	2	588.3	2	21.6	5	68.1	-5	8.4	8.7	9.8	13	1.84
ANA	350.4	13	745.3	14	39.7	133	109.9	58	11.3	5.5	13.0	13	2.03
UTHERN	2534.0	16	4949.6	20	308.5	6	562.9	9	12.2	13.3	13.3	13	1.72
UTHWESTERN PUBLIC SERVICE (4)	225.0	10	428.8	11	19.9	-25	38.0	-16	8.8	12.9	15.5	12	2.70
CO ENERGY	361.5	3	702.6	5	49.2	4	91.6	8	13.6	13.5	16.3	15	1.65
ICOM	1548.0	1	3231.9	3	120.8	-4	278.4	20	7.8	8.1	12.0	8	3.25
ION ELECTRIC	509.6	-1	969.0	1	63.9	-16	104.1	-9	12.5	14.8	12.7	14	2.85
SHINGTON WATER POWER	195.9	23	443.9	24	9.0	41	50.9	17	4.6	9.5	11.4	12	1.53
STERN RESOURCES	436.1	17	991.7	22	28.7	32	73.5	16	6.6	5.8	11.3	10	2.84
ICELABRATOR TECHNOLOGIES	366.0	-1	705.5	-5	49.8	-6	90.4	-7	13.6	14.3	9.1	20	0.73
SCONSIN ENERGY	401.7	-1	897.1	2	45.9	-12	109.0	-5	11.4	12.8	12.1	13	2.06
GAS, OIL & TRANSMISSION													
GROUP COMPOSITE	8397.2	29	20208.9	34	423.8	24	1318.3	15	5.0	5.3	8.3	22	1.55
DOCKLYN UNION GAS (3)	254.3	17	849.7	22	-4.5	NM	70.0	4	NM	NM	10.4	13	1.95
LUMBIA GAS SYSTEM	582.4	28	1785.4	20	8.2	-73	159.5	0	1.4	6.8	-28.8	NM	-8.75
STERN ENTERPRISES	214.6	8	633.9	12	9.9	40	42.8	14	4.6	3.6	15.3	10	3.22
PASO ENERGY	587.3	217	1192.9	206	24.4	21	-10.8	NM	4.2	10.9	4.7	42	0.96
BITABLE RESOURCES	391.8	24	1032.0	43	0.9	NM	39.7	49	0.2	NM	2.0	65	0.42
IN	356.9	36	1150.1	46	7.6	89	89.0	33	2.1	1.5	15.8	14	1.73
TIONAL FUEL GAS (3)	239.3	24	731.7	28	17.3	93	73.0	40	7.2	4.6	11.5	13	2.62
OR	336.5	36	1037.4	21	25.4	49	70.9	22	7.5	6.9	15.8	13	2.23
EOK (4)	289.7	4	754.4	28	11.7	30	50.3	35	4.0	3.0	13.1	13	2.06
IFIC ENTERPRISES	560.0	-7	1191.0	-2	59.0	23	113.0	18	10.5	8.0	14.7	12	2.34
ENERGY	1435.7	12	3148.7	25	79.6	18	181.6	20	5.5	5.3	14.5	14	2.22
DMONT NATURAL GAS (2)	259.5	45	498.6	31	32.5	35	66.5	23	12.5	13.4	12.8	13	1.82
NAT	847.2	78	1581.6	75	40.6	134	86.2	57	4.8	3.6	14.9	17	2.60
X-DELHI GROUP	212.0	52	484.5	75	-1.2	NM	1.2	-82	NM	1.7	-1.2	NM	0.11
ILICORP UNITED	765.0	27	1849.4	39	26.3	265	63.6	61	3.4	1.2	10.3	12	2.22
GOR	227.6	27	556.3	24	5.7	111	36.6	33	2.5	1.5	13.1	13	2.70
LIAMS	837.5	26	1731.2	33	80.4	-3	185.3	11	9.6	12.5	9.7	17	2.83

ALPHABETICAL LIST OF COMPANIES

The number following each company name identifies the Scoreboard category under which it is listed

10c ott Laboratories 12d Industries 21e Technologies 7b ptec 9d Telecomm. 22a be Systems 18c anced Micro 9d anta 17a O 21d 24a a 17b AC 17b anson (H.F.) 17c Products & Chemicals 4 orne Freight 23c ouch Communications 22a Steel Holding 16b aka Air Group 23a emarie 4 erto-Culver 6d ertson's 10c Standard 5 a 16a Brown 17a ander & Baldwin 23d ghany 17a gheny Ludlum 16b gheny Power 24a rigan 12b edSignal 5 late 17b el 22b max 16a erada Hess 11a erica West 23a erican Brands 6e erican Electric 24a erican Express 17a erican Freightways 23c erican General 17b erican Greetings 14d	American Home 12b American Intl Group 17b American Management Systems 18c American National 17b American Standard 13a American Stores 10c AmeriSource Health 12a Ameritech 22b Ames Dept. Stores 8 Ametek 9a Amgen 12b Amoco 11a AMP 9d Amphenol 9d AMR 23a Analog Devices 9d Andrew 9b Anheuser-Busch 6c Anixter International 5 Apache 11a APL 23d Apogee Enterprises 21a Apple Computer 18b Applied Materials 15c APS Holding 21b Arbor Drugs 12a Arcadian 4 Arco Chemical 4 Arkansas Best 23d Armstrong World 6b Arrow Electronics 21b Arvin Industries 2b Ashland 11a Associates First Capital 17a AT&T 22a AT&T Capital 17a Atlantic Richfield 11a Atmel 9d AutoZone 8 Avery Dennison 15a Avon Products 6d AVX 9d Aztar 14c	B Baker (J.) 8 Baker Hughes 11b Ball 7a Bally Entertainment 14c Baltimore G&E 24a Banc One 3b Bancorp Hawaii 3d Bandag 2c Bank of Boston 3a Bank of New York 3a BankAmerica 3d Bankers Trust 3a BanPonce 3c Bard (C.R.) 12d Barnes & Noble 8 Bausch & Lomb 12d Baxter International 12d Bay Networks 18c BDM International 18c Beckman Instruments 9c Becton-Dickinson 12d Bell & Howell 18a Bell Atlantic 22b BellSouth 22b Belo (A.H.) 20 Arcadian 4 Beneficial 17a Bergen Brunson 12a Best Buy 6b Best Products 8 Beverly Enterprises 12c Big B 12a Black & Decker 15b Blockbuster 17a Boatmen's Bancshares 3b Bob Evans Farms 14a Boeing 1 Boise Cascade 19a Boise Cascade Office Prods 21b Borders Group 8 Borg-Warner Automotive 2b Borg-Warner Security 21e	C Boston Edison 24a Boston Scientific 12d Bowater 19b Bradlees 8 Bristol-Myers Squibb 12b Brooklyn Union Gas 24b Brown Group 6a Brown-Forman 6c Brownings-Ferns 21c Bruno's 10c Brunswick 14d Burlington Northern Santa Fe 23b Burlington Resources 11a Butler Mfg 21a	C Cabletron Systems 18c Cabot 4 Cadence Design Systems 18c Caldor 8 Caliber System 23d Callaway Golf 14d Campbell Soup 18b Canandaigua Wine 6c Capital One Financial 17a Capstead Mortgage 13b Carlisle 15a Carnival 14d Carson Pirie Scott 8 Case 15c Casey's General Stores 10c Castle (A.M.) 21b Caterpillar 15c CDI 21e CDW Computer Centers 8 CellStar 21b Centener Energy 24a Central Fidelity Banks 3c Century Telephone 22a Ceridian 18c Champion Enterprises 13b Champion Intl 19b Charming Shoppes 8 Chase Manhattan 3a	C Chesapeake 19b Chevron 11a Chrysler 2a Cincinnati Bell 22b Cincinnati Financial 17b Cincinnati Milacron 15b Cintas 21e CipSCO 24a Circuit City Stores 6b Circus Circus 14c Circus Logic 9d Cisco Systems 18c Citicorp 3a CMS Energy 24a Coastal 11a Coca Cola 6c Coca-Cola Bottling 6c Coca-Cola Enterprises 6c Colgate-Palmolive 6d Collins & Aikman 15d Coltec Industries 15c Columbia Gas 24b Comdisco 18c Commerica 3b Commerce Group 17b Commercial Metals 16b Compaq Computer 18b CompuCom Systems 18a CompuServe 18c Computer Associates 18c Computer Sciences 18c Comsat 22a ConAgra 10b Cone Mills 15d Conrail 23b Consolidated Edison 24a Cons. Freightways 24a Consolidated Papers 19b Consolidated Stores 8 Continental Airlines 23a Continental Homes Holding 13b Cooper Industries 9a Cooper Tire & Rubber 2c Corning 15a	C Corporate Express 8 Countrywide Credit 17a CPC International 10b Cracker Barrel 14a Crane 21b Crestar Financial 3c Crown Central Petroleum 11a Crown Cork & Seal 7a CSX 23b CUC International 21e Cummins Engine 2b Cyprus Ammax Minerals 16c Cytec Industries 4	D Dana 2b Danaher 15b Darden Restaurants 14a Dayton Hudson 8 Dean Foods 10b Dean Witter, Discover 17a Deere 15c Dell Computer 18b Delta Air Lines 23a Deluxe 18a Detroit Diesel 2b Dexter 4 Dial 5 Diamond Shamrock 11a Diebold 18a Digital Equipment 18b Dillard's 8 Disney (Walt) 14b Dole Food 10b Dollar General 8 Dominion Resources 24a Donaldson 2b Donaldson, Lufkin & Jenrette 17a Donnelly (I.R.) 21d Dover 15c Dow Chemical 4 Dow Jones 20 DPL 24a Dresser Industries 15c	D Drug Emporium 12a DSC Communs 22a DTE Energy 24a Duke Power 24a Dun & Bradstreet 20 DuPont 4 Duracell International 15a
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ALPHABETICAL LIST OF COMPANIES

The number following each company name identifies the Scoreboard category under which it is listed

General Electric 17a General Motors 15a Federal Mogul 2b Federated Dept. Stores 8 Ferro 4 First Interstate 15d First Third Bancorp 3b First Union 8 First American Finl 17a First Bank Systems 3b First Interstate Finl 3b First Union 18c First Empire State 3a First Maryland Bancorp 3a First of America Bank 3b First Security 3d First Tennessee Natl 3c First Union 3c Fidelity 3b Fidelity 18c Fleet Financial Group 3a Fleetwest 14d Florida Progress 24a Fluor 21a FMC 15c Fonar International 15a Ford 10c Foodbrands America 10b Foodmark 14a Ford Motor 2a Fort Howard 19b FPL Group 24a Freeport-McMoran 2c Freeport-McMoran C&G 16c Fremont General 17b Frontier 22b Fruit of the Loom 6a Fuller (H.B.) 4 G General 20 Gap 8 Gateway 2000 18b GATX 23c Gaylord Container 7b GenCorp 2b General 12b General Electric 1 General Electric 5 General Instrument 9b General Mills 2a General Motors 10a General Nutrition 10c General Public 24a General Signal 9a General Signal 12a Genuine Parts 21b Geon 4 Georgia Gulf 4 Georgia Pacific 19a Georgia-Pacific 21b Grant Food 10c Grain Processing 15b Grain Processing 6d Grain Processing 17c Goodrich (B.F.) 4 Goodyear Tire & Rubber 2c Goodyear Tire & Rubber 12b Great A&P 10c Great Lakes Chemical 4 Great Western 17c Great Western 17a Great Western 15a Great Western 22b Glech Holdings 18c Glech Holdings 12d Guilford Mills 15d H Handleman 21e Harcourt 10c Harcourt General 5 Harley-Davidson 14d Harsco 15c Harrish's Entertainment 14c Harsco 9b Harsco 15a Harsco 24d Hawaiian Electric 24a Hawaiian Electric 12c	Health Management Assoc. 12c Healthsouth 12c Hechinger 8 Hering-Meyers 6b Hercules (H.) 10b Hercules 4 Hemlock Ind. 10b Hewlett-Packard 18b Hill 21e Hillenbrand 15a Hills Stores 8 Hilton Hotels 14c Home Depot 8 Home Shopping 8 HON Industries 18a Honeywell 9c Hugoboss 19b Hormel Foods 10b Host Marriott Services 14a Houghton Mifflin 20 Household Int'l 17a Hubbell 9a Hudson Foods 10b Huffy 14d Hughes Electronics 9b Hughes Supply 21b Hunt (J.B.) 23d Huntington Bancshares 3b I IBM 18b IBM 10b IBM 15a InaCom 21e Informix 18c Ingersoll Rand 15c Inland Steel 16b Integrated Health Svcs 12c Intel 9d Intellectual Electronics 18a Intergraph 18c Interim Services 21e International Flavors 4 International Game Tech 15a Intl. Multi-Foods 10a International Paper 19b Intl. Specialty Foods 4 Interstate Bakeries 10b Intimate Brands 8 Interlogix 18b ITT 14c ITT Industries 5 J Jacobs Engineering 21a Jacobs 19b Jefferson Smurfit 7b Johnson & Johnson 12d Johnson & Johnson 15a Johnson & Johnson 6a K K-III Communications 20 Kaiser Aluminum 16a Kaman 21b Kansas City Power & Light 24a Kansas City Southern 23b Kaiser Aluminum 10c Kaiser Aluminum 10b Kellwood 6a Kellwood 15b Kellwood 19b Kmart 8 Knight-Ridder 20 Kroger 10c L Lafarge 13a Lands' End 8 Landstar System 23d LCI International 22a Lear 2b Leggett & Platt 6b Lehrman Brothers Holdings 17a Lennar 13b Levitz Furniture 6b Lexmark Intl. Group 18b Libby (H.J.) 12b	Limited 8 Lincoln Electric 15b Lincoln National 17b Litton Industries 9b Liz Claiborne 6a Lockheed Martin 1 Lodite 4 Longs Drug Stores 12a Longview Fibre 7b Louisiana Land 11a Lumbar Pacific 19a Lowe's 8 LSI Logic 9d LTV 16b Lubrizol 4 Lucent Technologies 22a Lubrizol 16b Lyondell 4 M Mail-Well 7b Manor Care 12c Mark IV Industries 15a Marriott Intl 14c Marsh & McLennan 17a Marshall & Ilsley 3b Marshall Industries 21b Martin Marietta Materials 13a Mattel 14d Maxxim 16a May Department Stores 8 Maytag 6b MBNA 3a McGraw-Hill 10b McDonald's 14a McDonnell Douglas 1 McGraw-Hill 20 MCI Communications 22a McKesson 12a MCN 24b M.D.C. Holdings 13b Mead 19b Medaphis 21e Media General 20 Medtronic 12d Mellon Bank 3a Mellon 12a Mercantile Bancorporation 3b Mercantile Stores 8 Merrill Lynch 17a Meyer (Fred) 8 MGIC Investment 17b MGM Grand 14c MGM Resorts 8 Micro Warehouse 8 MicroAge 18a Micron Electronics 18b Micron Technology 9d MicroSoft 18c MidAmerican Energy 24a Miller (Herman) 18a Mirage Resorts 14c Mitchell Energy 11a Modine 11a Modine Mfg. 2b Mohawk Industries 15d Money Store 17a Monsanto 4 Montana Power 24a Morgan (J.P.) 3b Morgan Stanley 17a Morgan Stanley 9b Mueller Industries 16c Mueller 11a N Nabisco Holdings 10b Nabors Industries 11b Nacco Industries 15b Nash Finch 10a National City 3b National Fuel Gas 24b National Fuel Gas 9d National Service 9a National Steel 16b National Steel 3c Navistar International 2a Navistar 6d Neiman Marcus Group 8 Nevada Power 24a New England Electric 24a New York State E&G 24a	New York Times 20 Newell 15a NGC 11a Nico 24b Nike 6a Nine West Group 6a NL Industries 4 Noble Affiliates 11b Nordstrom 8 Norfolk Southern 23b Norrell 21e Nortek 13a Northeast Utilities 24a Northern States 24a Northern Trust 3b Northrop Grumman 1 Northwest Airlines 23a Norwest 3b Novell 18c NuCor 16b Nyne 22b O Oakwood Homes 13b Occidental Pet 11a Office Depot 8 OfficeMax 8 Ohio Edison 24a Old Kent Financial 3b Olin 4 Omicron Group 21d Oneok 24b Oracle 18c Orange & Rockland Uts. 24a Oregon Steel Mills 16b Orinda HealthCorp 12c Outback Steakhouse 14d Outboard Marine 14a Owens & Minor 12d Owens Corning 13a Owens-Illinois 7a P Packard 2a Pacific Enterprises 24b Pacific G&E 24a Pacific Telesis Group 22b PacificCare Health 12c PacificCorp 24a PaineWebber Group 17a Pall 5 PanEnergy 24b Panasonic 8 Payless ShoeSource 8 PECO Energy 24a Penn Traffic 10c Penney (J.C.) 8 Pentair 15c Pep Boys 8 PepsiCo 6c Perkin-Elmer 9c Petersmart 8 Pharm 12b Pharm 16c Pharm 21e Pharm 6e Pharm 11a Pharm 6a PhyCor 12c Piedmont Natural Gas 24b Pier 1 Imports 6b Pittsburgh 10b Pittsburgh 21e Pinnacle West 24a Pioneer Hi-Bred 10b Pioneer-Standart 21b Pitney Bowes 18a Pittsburgh-Brown Group 21e Pittsburgh Burlington Group 23c Pittway 5 Pittsburgh Industries 13a PNC Bank 3a Pittsburgh Industries 15a Polaroid 14d Portland General 24a Potlatch 19b PPG Industries 13a PP&L Resources 24a Praxair 4 Premark Intl. 5 Price/Costco 8 Price/Costco 17b	PS Co. of Colorado 24a PS Co. of New Mexico 24a Public Service Ent. 24a Puget Sound Power 24a Pulte 13b Q Quaker Oats 10b Quaker State 11a Qualcomm 9b Quality Food Centers 10c Qualex 16b R Raychem 9a Raymond James Finl. 17a Raytheon 19a Raytheon 9b Read-Rite 9d Reebok International 6a Regions Financial 3c Republic New York 3a Revco D.S. 12a Rexel 21b Reynolds & Reynolds 18a Reynolds Metals 16a Rhône-Poulenc Rorer 12b Richfield Holdings 10a Rite Aid 12a RJR Nabisco 6e Roadway Express 23d Rock-Tenn 7b Rockwell International 5 Rohm & Haas 4 Rohr 1 Rollins 21e Ross Stores 8 Rouge Steel 16b Royal Caribbean Cruises 14d RPM 13a Rubbermaid 15a Ruddick 10c Russell 6a Ryder System 23c Rykoft Sexton 10a Ryland Group 13b S Sabco 17b Safeguard Scientifics 18c Safety-Kleen 21e Safeway 10c Saks Holdings 8 Sallie Mae 17a Salomon 17a SBC Communications 22b Scana 24a Schering-Plough 12b Schlumberger 11b Scholastic 20 Schuller 19b Schulman (A.J.) 4 Schwab (Charles) 17a Scotts 4 Scripps (E.W.) 20 Seagate Technology 18b Sealed Air 15a Sears, Roebuck 8 Service Corp. Intl. 21e Service Merchandise 8 ServiceMaster 21e Shaw Industries 15d Sherwin-Williams 13a Shoney's 14a ShopKo Stores 8 Smart & Final 10a Smith (A.O.) 2b Smith International 11b Smith's Food & Drug 10c Smithfield Foods 10b Snap-on 15b Soletron 9d Sonata 24b Sonoco Products 7b Southern 24a Southern National 3c Southern New Eng. Tel. 22b Southern Pacific Rail 23b Southwest Airlines 23a Southwestern PS 24a Spiegel 8 Sports Authority 8 Springs Industries 15d	Sprint 22a SPX 15b St. Jude Medical 12d Standard Federal Bancorp 17c Standard Motor Prods. 2b Standard Register 18a Stanley Works 15b Staples 8 State Street Boston 3a Sterling Chemicals 4 Stewart & Stevenson 15c Stone & Webster 21a Stone Container 7b Stop & Shop 10c Strawbridge & Clothier 8 Stryker 12d Summit Bancorp. 3a Sun 11a Sun Microsystems 18b SunAmerica 17b Sunbeam 6b Sundstrand 1 SunTrust Banks 3c Super Food Services 10a Supermarkets Gen 10c Supervalu 10a Sybase 18c T Talbots 8 Tandem Computers 18b Tandy 6b TFC Financial 17c Tech Data 18a Teco Energy 24a Tecomseh Products 13a Tektronix 9c Teleline 5 Teleflex 15a Telephone & Data Sys. 22a Tellabs 22a Temple-Inland 7b Tenneco 5 Tenneco 9c Terra Inds. 4 Texaco 11a Texas Industries 13a Texas Instruments 9d Texton 5 Thomas & Betts 9a 3Com 18b 360 Communications 22a Tidewater 11b Tiffany 8 TIG Holdings 17b Time Warner 20 Times Mirror 20 Timken 15c TJX 8 Toro 6b Tosco 11a Toys 'R' Us 8 Transamerica 17b Travelers Group 17a Tribune 20 Trinity Industries 23c Trimova 15a Trump Hotels 14b TRW 5 Tupperware 15a Tyco Intl 15c U U.S. Bancorp 3d U.S. Can 7a U.S. Cellular 22a U.S. Healthcare 12c U.S. Home 13b U.S. Office Products 8 U.S. Robotics 24a U.S. Surgical 12d UAL 23a UCAR International 9a Ultrasim 11a Unicom 24a Unifit 15d Union Camp 7b Union Carbide 4 Union Electric 24a Union Pacific 23b Union Pacific Resources 11a Union Texas 11a	UnionBanCal 3d Unroyal Chemical 4 Unisys 18b United Asset Mgmt. 17a United Technologies 1 Unistrut 17b Univar 21b Universal Foods 10b Universal Forest Products 19b Universal Health 12c Unocal 11a UNUM 17b US West Communications 22b USAir Group 23a USFreightways 23d USF&G 17b USG 13a USLife 17b UST 6e USX-Delhi Group 24b USX-Marathon 11a USX-U.S. Steel 16b UtiliCorp United 24b V Valero Energy 11a Valspar 13a Value City 8 Vansair 18c Varian Associates 9b Varity 15c Vastar Resources 11a Vencor 12c Venture Stores 8 VF 6a VLSI Technology 9d Voll Info. Sciences 21e Vons 10c Vulcan Materials 13a VWR Scientific Products 21b W Waban 8 Wachovia 3c Wal-Mart Stores 8 Wallgreen 12a Wallace Computer 18a Walter Industries 16b Wang Laboratories 18c Warner-Lambert 12b Washington Post 20 Washington Water Power 24a Weatherford Enterra 11b Webb (Del.) 13b Wenton Steel 16b West Markets 10c Wellman 4 Wells Fargo 3d Western Atlas 11b Western Digital 18b Western Resources 24a WestPoint Stevens 6a Westvaco 19b Weyerhaeuser 19b Wheelabrator Techs 24a Whirlpool 6b Whitman 5 Wickes Lumber 8 Wicor 24b Wilamette Industries 19a Williams 24b Wisconsin Energy 24a WMX Technologies 21c Wolverine Tube 16c Woolworth 8 Worthington Inds. 16b Wrigley (Wm.) 10b Wye Electronics 21b XYZ Xerox 18b Yellow 23d York Intl 13a York 8 Ziegler Coal Holding 11a Zenith Electronics 6b
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EDITED BY AMY DUNKIN

THE BEST MOVES IF YOU'RE BROKE

Bad legal advice left one former entrepreneur saddled with \$150,000 in outstanding debt and no way to pay it. Told that it wouldn't make sense to incorporate her new management consulting firm, the woman ended up regretting that decision when business went south. "I started using my credit cards to keep the company alive," she says. In 1991, after seven years in business, she closed the doors. It only got worse, however. Creditors harassed her, and lawsuits ensued. "I decided to file for bankruptcy to protect my future," she says. "I'm not alone. Well over

1 million people are expected to file for bankruptcy this year, an all-time high, according to the American Bankruptcy Institute (ABI). "Consumer bankruptcy is not just for deadbeats: It includes a wide range of incomes," says Samuel Gerdano, executive director of the ABI, a nonprofit research group. So far, more than 266,000 consumers filed in the first quarter of this year, up 25% over the same period last year. Explains Melvin Kaplan, a Chicago-based bankruptcy attorney: "Bankruptcy no longer carries as bad a stigma as it once did."

Easier access to credit,

coupled with corporate layoffs, have helped fuel the rise in bankruptcies. Consider the recent explosion of credit availability: There were 5 billion credit-card solicitations, or 32 invitations for each American aged 18 to 64, between 1994 and 1995. As a result, monthly consumer debt service has climbed to a near-record 17% of disposable personal income this year. For many people, the simplest means of getting out from under a growing mountain of debt is to declare bankruptcy. There are two different types of filings for individuals: Chapter 7 and Chapter 13.

QUICK ROUTE. Chapter 7, also known as straight bankruptcy, requires financially troubled folks to submit most of their assets to the bankruptcy trustee, who then sells them and distributes the proceeds to the creditors as partial payment on the debt. Debtors are allowed to keep certain non-exempt assets, which are determined by the

various state codes or federal code. These usually include clothing, household appliances, furnishings, life insurance, pensions, and sometimes a home or car. Chapter 7 process usually takes four to six months, after which the entire debt load is forgiven and debtor is discharged. Chapter 7 cannot be filed again for another six years.

Chapter 13, which is called the wage-earner option, is a debt reorganization recipe that can last up to five years. Instead of turning over assets, debtors with a steady income can submit partial that income for distribution among creditors to pay all or a portion of their debts under court protection. The amount that is repaid is negotiated then court-approved. Once the repayment plan has been completed, the consumer debt is discharged. There is no restriction on when a person can file again.

The moment any type of bankruptcy is filed with the courts, all collection efforts and legal actions must stop. The consumer gets immediate relief and protection from creditors and the pressure of the mounting debt. "The individual gets a fresh financial start," says Norton Hammes, a bankruptcy attorney in San Jose, Calif. Whether both filings, however, there are some debts that can't be forgiven, including alimony, child support, the last three years of income taxes, and most student loans less than seven years old.

But there's a downside: bankruptcy shows up on credit report for 10 years or seven years if a Chapter 13 repayment plan has been completed. It may be difficult to secure a mortgage, rent an apartment, obtain a credit card, and—despite laws to the contrary—get hired by some companies.

Ironically, once you have filed for bankruptcy, you may still be able to get some credit, but you'll almost certainly pay a steep interest rate

eight percentage points. In fact, according to a study by Purdue University's Credit Researcher, 17% of people who for Chapter 7 obtained within one year of fil-

by agreeing to pay down debt in installments with interest. The good news is that you'll be able to hold onto the property and salvage your credit report. The trade-off is that the debtor may end

amount is determined in negotiations.

Of course, the difficult question of whether to seek any type of bankruptcy relief should not be taken lightly. All other alternatives for handling problem debt should be considered first. "Bankruptcy should be the last resort," advises David Doyaga, a New York-based bankruptcy attorney.

Indeed, if your credit history isn't wounded beyond repair, it may be possible to take out a large, low-interest loan to pay off higher-interest debt. That way the debt is consolidated into one payment. Another option is to try to negotiate directly with creditors. Debtors may be able to settle for a smaller cash payment, extend the payment period, or suspend additional interest payments while the debt is paid off.

Sometimes creditors won't deal with problem consumers.

Under that scenario, it's best to visit a credit counselor at a nonprofit agency who may be able to work out a restructured payment plan with creditors. Counselors can also help consumers learn how to budget and track expenses so debt problems can be avoided in the future. The nonprofit National Foundation for Consumer Credit (800 388-2227), with 1,197 Consumer Credit Counseling Service offices nationwide, can help consumers resolve problems through a debt-management plan for a low-cost fee of about \$9 a month. Universities also provide nonprofit credit-assistance programs.

WARNING FLAGS. When the signposts are all too clear—your credit rating is a mess, you've been paying debt for six months without reducing the balance, or you're borrowing off of one card to pay off another—then seeking bankruptcy protection may

be prudent. "For some people, bankruptcy is a sensible decision," notes Robert Johnson, senior research associate at the Credit Research Center. At that point, call the nearest bankruptcy court for a list of attorneys who act as trustees and file Chapter 7 and 13 cases. Or contact the American Bankruptcy Board of Certification (703 739-1023) for referrals. Another resource: The American Bar Assn. sells a videotape and accompanying booklet, *Dealing with Debt: Bankruptcy and Other Options* for \$49 (312 988-5522).

The best suggestion, of course, is to avoid excessive debt in the first place. Or try to negotiate with your creditors. You'll feel better about repayment, and so will they. *Toddi Gutner*

FINANCES Even after filing for bankruptcy, you may still be able to get credit, but at a steep rate

Credit-card companies charge the higher interest rates to cover the increased cost of offering credit to riskier borrowers.

Determining the best type of protection to seek depends on the type and total net of assets and whether an individual has a steady income. About 70% of those who go into bankruptcy file under Chapter 7.

LAW. Chapter 7 is more appropriate for individuals who have few assets to protect. These are people who don't usually own a home or car and have an already-paid-for car. Whatever remaining assets they have are typically sold. Certain states such as Florida and Texas let people have unlimited home equity protection, although most states cap on the exemption. New York, for example, only allows \$10,000 of protection for home equity. Creditors can take the home, sell it, keep whatever proceeds exceed \$10,000.

If a creditor is going, an individual may be able to keep exempt assets such as a home or car

up paying more than the property is currently worth.

Those with many possessions should probably consider a Chapter 13, which allows debt-laden borrowers to keep all of their assets. But the consumer must pay off at least as much as the creditors would have gotten in a Chapter 7 bankruptcy. That

Alternatives For Consumers With Financial Woes

ISSUE	CHAPTER 7 LIQUIDATION	CHAPTER 13 PARTIAL REPAYMENT
DEBT RESTRICTIONS	None	Maximum of \$750,000 secured debt, \$250,000 unsecured
INCOME REQUIREMENTS	None	Must have regular income, be able to make required payments
INTEREST STOPPED ON CREDIT CARDS	Yes	Yes
STOPS CREDITOR HARASSMENT, GARNISHMENTS, LAWSUITS	Yes	Yes
STOPS IRS OR STATE INCOME TAX GARNISHMENTS	Temporarily for recent-year taxes*	Yes; recent taxes can be repaid, usually with no interest or penalties after filing date; older taxes can be discharged
STOPS HOME FORECLOSURES	Temporarily	Yes; past-due payments can be repaid over 3-5 years
STOPS CAR REPOSSESSIONS	Temporarily	Yes; loan can sometimes be reduced and payments restructured through the plan
AMOUNT IN PERSONAL ASSETS DEBTOR CAN KEEP	As allowed by each state	As allowed by each state; if amount exceeds maximum, debtor can pay excess to unsecured creditors over 3-5 years
LENGTH OF TIME ON CREDIT REPORT	10 years from filing date	10 years from filing date; if plan is completed may be removed in 7 years
COURT FEES	\$175	\$160
ATTORNEY FEES	\$500-\$1,000	\$1,000-\$2,000

* Some older taxes can be discharged

DATA: NATIONAL ASSOCIATION OF CONSUMER BANKRUPTCY ATTORNEYS

'HOW WOULD YOU LIKE YOUR OSTRICH BURGER?'

If beef alternatives such as chicken and fish leave you yearning for sirloin, it may be time to stick your neck out and try a new poultry dish: barbecued ostrich. Like beef, it's red meat, but much lower in fat and calories. There's just one problem—it's a lot more expensive.

Europeans have been eating ostrich for years, but until 1992, it couldn't easily be found in the U.S. With trade bans lifted, ostriches imported from South Africa are being bred and slaughtered here. Breeder Chip Polvoorde, president of Brandywine Meats in Escondido, Calif., believes there are at least two dozen big ranch-

es in the U.S. with 1,000 or more birds. At larger breeders, the birds graze on alfalfa supplemented with corn and vitamins. Owners slaughter the ostriches between 9 and 16 months of age. Older birds, like older cattle, yield tougher meat.

Ostrich has an outstanding nutritional profile that's similar to American bison. A 100-gram cooked portion of lean ostrich meat has about the same protein content as beef, 27% to 30%.

But the ostrich has one-third fewer calories—142—than beef, which has 211, according to government and university studies. Ostrich also has two-thirds less fat, just 3 grams, than its bovine rival, which has 9.3 grams. "Cardiologists have given ostrich two thumbs

up," says Doug Hendrix, a spokesman for Von's, the supermarket chain that carries the meat of this big bird at its 32 Pavilion stores in California.

LOW-FAT. Dark brown when raw, some ostrich cuts are almost liver-like in appearance. You'll find no fat to trim from the edges—or to add to weight and cost—and none is "marbled" into the meat. Lacking fat, ostrich will provide more nutrition than beef. But this meat doesn't give you that long-lasting "full" feeling you get from eating slower-to-digest fatty foods. Because ostrich is so lean, much of its flavor must be accented with spices such as

pepper and garlic powder, or Worcestershire sauce on the cooked bird. Marinating is a good idea because it tenderizes as well.

Ostrich cooks faster than other meats, and thin steaks and fillets toughen if overcooked. So approach it as you would veal, and don't even think about trying it well-done.

Steaks should be cooked medium-rare to medium (to an internal temperature of 140 to 160 degrees). Place half-inch cuts closer to the coals or heat source and cook each side for three to five minutes, advises food consultant Sandra Hildreth, who learned the hard way. She bought a large order of ostrich steaks for a barbecue party, then under-

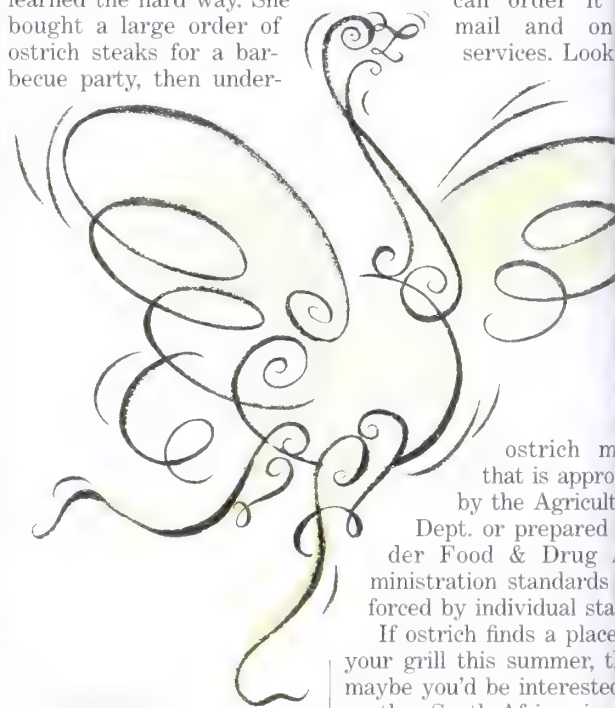
\$30, 817 447-6964 to order.

What you taste with a mouthful of ostrich depends partly on preparation, partly on perception. "It tastes more like steak than chicken," says Tammy Baker, a registered dietitian based in Phoenix. Other people say ostrich reminds them of duck.

FOOD

Even the ostrich prices at least twice those of beef. Fillets and steaks are \$10 and \$15 a pound; roasts \$10 to \$11; and ground meat and sausage are \$4 to \$5. Few major supermarket chains stock ostrich, but you can find it at a growing number of specialty shops.

You can order it by mail and online services. Look



ostrich meat that is approved by the Agriculture

Dept. or prepared under Food & Drug Administration standards enforced by individual states.

If ostrich finds a place on your grill this summer, maybe you'd be interested in another South African import that ranchers are breeding to offer as another alternative to beef: Boer goat. In many backyards, barbecued burgers just may never be the same. *Richard Korman*

Where To Order

BRANDYWINE MEATS

Escondido, Calif., 619 489-7900
Ships only in California

HEARTLAND OSTRICH RANCH

Owensville, Ind., 812 724-BIRD
Introducing marinated frozen ostrich steak for \$11 a pound

NEW ENGLAND OSTRICH

Whatley, Mass., 413 665-BIRD
Ships all cuts; offers Ostrich Osti Kielbasi and hot dogs

OSTRICH VISION

Roslyn, N.Y., 516 621-5470
Specializes in fillets and steaks; minimum, 5 pounds or \$100

OSTRICHES ON LINE

Elmwood Park, Ill., 708 452-7596
<http://www.achiever.com/ostich>
Takes minimum \$25 orders of USDA-inspected meat

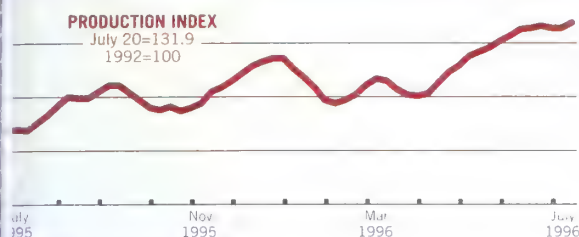
WORTH NOTING

■ **FINANCIAL HELP.** Small-business owners can learn about government and private-sector funding sources a 154-page booklet from MasterCard International, *The Small Business Financial Resource Guide*. Free copies may be obtained from the U.S. Chamber of Commerce (202 463-5503) and the National Association of Women Business Owners (800 556-2926).

Business Week Index

PRODUCTION INDEX

Change from last week: 0.4%
Change from last year: 7.6%



The production index increased in the week ended July 20. After seasonal adjustment, production of autos rebounded as car makers' summer shutdowns ended, although truck output dipped. Other gainers were steel, electric power, paper, and paperboard. Crude-oil refining, coal, lumber, and rail-freight traffic all declined. Before calculation of the four-week average, the index rose to 132 from 132 the week before.

Leading index will be unavailable for an indefinite period.

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (7/26) S&P 500	635.90	638.73	13.3
PORTRAIT BOND YIELD, Aaa (7/26)	7.79%	7.79%	1.3
INDUSTRIAL MATERIALS PRICES (7/26)	106.8	106.3	-5.9
BANKRUPTCY FAILURES (7/19)	NA	NA	NA
REAL ESTATE LOANS (7/17) billions	\$521.9	\$521.8	6.2
VEHICLE SUPPLY, M2 (7/15) billions	NA	NA	NA
UNEMPLOYMENT CLAIMS, UNEMPLOYMENT (7/20) thous	367	367	-21.7

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (7/30)	5.33%	5.25%	5.83%
COMMERCIAL PAPER (7/30) 3-month	5.54	5.50	5.80
CERTIFICATES OF DEPOSIT (7/31) 3-month	5.55	5.51	5.75
FIXED RATE MORTGAGE (7/26) 30-year	8.40	8.44	8.06
ADJUSTABLE RATE MORTGAGE (7/26) one-year	6.10	6.21	5.94
LIBOR (7/30)	5.25	5.25	5.75

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

All data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

LEADING INDICATORS

Friday, Aug. 5, 8:30 a.m. EDT ▶ The Conference Board is expected to report that its composite of leading indicators rose 0.2% in July, according to the median projection of economists surveyed by MMS International, a unit of The McGraw-Hill Companies. The index gained 0.3% in May. The expected advance would mark the fifth consecutive increase, the first time that has happened in more than two years.

FEDERAL RESERVE BOOK

Wednesday, Aug. 7, 12 noon EDT ▶ The Federal Reserve will release the results of its periodic survey of business conditions in all of its 12 districts. The report is pre-

pared for use at the upcoming policy meeting on Aug. 20. The previous Beige Book noted generally moderate economic growth with low inflation, but it also pointed to a quickened pace of activity and tightening labor markets in some regions. Fed officials will be on the watch for any broadening of those conditions.

CONSUMER CREDIT

Wednesday, Aug. 7, 3 p.m. EDT ▶ The Federal Reserve is expected to report that consumer installment debt increased by \$7.5 billion in June, following a \$4.7 billion rise in May. Credit growth slowed substantially from February to May, after monthly gains averaging \$11.4 billion in 1995. The run-

up in credit-card debt, which accounted for half of the growth in installment credit from 1993 to 1995, is beginning to slow. And excluding revolving credit, consumers actually liquidated debt in both April and May for the first time in more than three years. Given strong income growth, the ratio of debt to income may have peaked.

PRODUCER PRICE INDEX

Friday, Aug. 9, 8:30 a.m. EDT ▶ The Labor Dept. is expected to report that producer prices for finished goods in July rose 0.2%, according to the MMS survey, following a 0.2% increase in June. The core index, excluding energy and food, is also projected to rise 0.2%, also the same as in June.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (7/27) thous. of net tons	1,964	1,939#	3.9
AUTOS (7/27) units	117,570	113,094r#	5.1
TRUCKS (7/27) units	102,946	92,682r#	2.4
ELECTRIC POWER (7/27) millions of kilowatt-hrs	72,804	73,630#	-6.6
CRUDE-OIL REFINING (7/27) thous. of bbl./day	14,092	14,141#	1.2
COAL (7/20) thous. of net tons	18,982#	18,045	4.9
PAPERBOARD (7/20) thous. of tons	920.0#	868.8r	1.2
PAPER (7/20) thous. of tons	797.0#	768.0r	-3.7
LUMBER (7/20) millions of ft.	471.0#	457.2	7.7
RAIL FREIGHT (7/20) billions of ton-miles	25.8#	24.7	2.0

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWPAI, SFPAA, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (7/31) \$/troy oz.	385.300	384.400	0.5
STEEL SCRAP (7/30) #1 heavy, \$/ton	133.50	133.50	-5.0
COPPER (7/27) ¢/lb.	96.5	91.3	-29.8
ALUMINUM (7/27) ¢/lb.	70.0	68.5	-20.9
COTTON (7/27) strict low middling 1-1/16 in. ¢/lb.	77.01	77.55	-12.8
OIL (7/30) \$/bbl.	21.43	21.67	21.9

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, ENR

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (7/31)	106.77	107.93	91.04
GERMAN MARK (7/31)	1.47	1.49	1.39
BRITISH POUND (7/31)	1.56	1.55	1.60
FRENCH FRANC (7/31)	5.00	5.03	4.81
ITALIAN LIRA (7/31)	1519.2	1516.0	1582.2
CANADIAN DOLLAR (7/31)	1.37	1.37	1.36
MEXICAN PESO (7/31)	7.576	7.608	6.140

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

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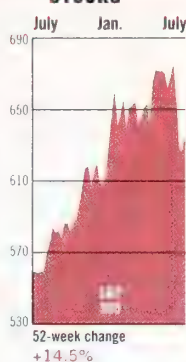
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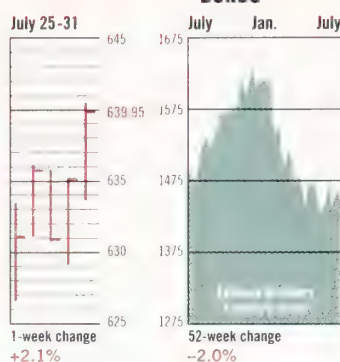
STOCKS

Stocks began a fitful climb as the lows the major indices ended on July 23 and 24. The Jones industrial average edged nearly 100 points during the week to 5528.9 on July 31, as lower interest rates credited the gains. Yields of benchmark Treasury bills fell to 6.97% on July 31, after rising as high as 7.25% two days before. But the decline caused the dollar to slip to a two-month low against the mark and a five-month low vs. the yen.

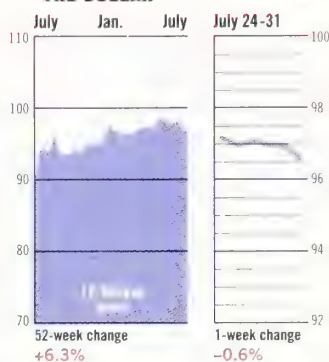
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change	
		Week	52-week
JONES INDUSTRIALS	5528.9	3.3	17.9
DOE COMPANIES (S&P MidCap Index)	219.8	2.5	7.2
DOE COMPANIES (Russell 2000)	316.0	2.7	6.1
DOE COMPANIES (Russell 3000)	362.0	2.3	13.1

IGN STOCKS	Latest	% change (local currency)	
		Week	52-week
FIN (FINANCIAL TIMES 100)	3703.2	0.9	5.8
NIKKEI INDEX	20,692.8	0.3	23.8
TSE COMPOSITE	4929.0	1.0	7.3

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.30%	5.30%	5.57%
30-YEAR TREASURY BOND YIELD	6.97%	7.04%	6.86%
S&P 500 DIVIDEND YIELD	2.24%	2.29%	2.39%
S&P 500 PRICE/EARNINGS RATIO	18.3	18.0	16.4

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	635.0	633.7	Positive
Stocks above 200-day moving average	42.0%	38.0%	Neutral
Speculative sentiment: Put/call ratio	0.68	0.71	Neutral
Insider sentiment: Vickers sell/buy ratio	2.10	2.21	Neutral

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

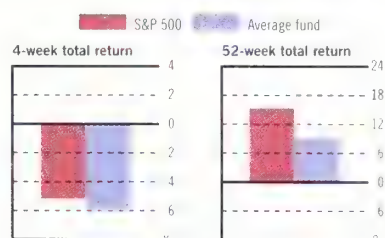
MONTH LEADERS		% change		Strongest stock in group	% change		Price
		1-month	12-month		1-month	12-month	
HOUSEWARES		2.8	9.6	RUBBERMAID	5.5	-3.0	28 ³ / ₄
DES		0.5	74.5	REEBOK INTERNATIONAL	4.5	-3.4	35 ¹ / ₂
COMMERCIAL SERVICES		0.5	21.8	OGDEN	4.1	-14.2	18 ¹ / ₂
KEY CENTER BANKS		0.0	30.0	BANKAMERICA	5.0	46.9	79 ¹ / ₂
REST PRODUCTS		-0.2	-12.4	LOUISIANA-PACIFIC	-9.0	-23.3	20 ¹ / ₂

MONTH LAGGARDS		% change		Weakest stock in group	% change		Price
		1-month	12-month		1-month	12-month	
CKING		-26.5	-39.5	CALIBER SYSTEM	-45.2	-56.6	18 ⁵ / ₈
CHINE TOOLS		-21.6	-34.1	GIDDINGS & LEWIS	-29.2	-32.9	11 ¹ / ₂
Os		-17.6	4.9	UNITED HEALTHCARE	-33.2	-25.0	33 ³ / ₄
ILINES		-16.8	-5.9	SOUTHWEST AIRLINES	-20.6	-18.1	23 ¹ / ₂
ENSE ELECTRONICS		-16.4	37.7	EG&G	-16.4	-2.7	17 ⁷ / ₈

MUTUAL FUNDS

LEADERS		LAGGARDS	
4-week total return	%	4-week total return	%
PSTONE NEW ZEALAND	2.3	PREMIER STRATEGIC GROWTH C	-18.6
IA HOUSE FAR EAST GROWTH	1.0	FIDELITY SELECT AIR TRANSPORTATION	-18.3
M SAMI PREFERRED STOCK INCOME	0.5	KEYSTONE AMERICA HARTWELL EMERG. GR. B	-17.5

52-week total return	%	52-week total return	%
NDMARK SMALL CAP EQUITY A	60.0	STEADMAN TECHNOLOGY GROWTH	-39.0
UNITREND GOLD	50.1	SELIGMAN COMMUNICATIONS & INFORM. D	-26.8
EMONT U.S. MICRO-CAP	41.2	STEADMAN AMERICAN INDUSTRY	-26.7



RELATIVE PORTFOLIOS

Amounts represent the net value of \$10,000 invested one year ago in each portfolio.

Percentages indicate daily total returns.

U.S. stocks
\$11,625
+1.34%

Foreign stocks
\$10,869
-0.45%

Money market fund
\$10,527
+0.11%

Treasury bonds
\$10,346
-0.82%

Gold
\$10,073
+0.08%

Data on this page are as of market close Wednesday, July 31, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of July 30.

Mutual fund returns are as of July 26. Relative portfolios are valued as of July 30. A more detailed explanation of this page is available on request. r= revised

THE RIGHT WAY TO CUT TAXES

It is easy to be cynical when vote-hungry politicians talk tax cuts at election time. But the dramatic 10%-to-15% tax cuts being discussed by GOP candidate Bob Dole deserve serious—and careful—consideration. We believe that a cut in marginal income tax rates can spur higher economic growth. We believe, as well, that this growth can generate some of the revenues lost to the Treasury. We worry, however, that politicians will confuse cutting taxes with fiscal responsibility. We're concerned about the new silence in Washington surrounding runaway entitlement spending and the loose talk of tax cuts fully paying for themselves. In a quarter when business profits are healthy, inflation remains subdued, and economic growth purrs along, the last thing this nation needs is a replay of the 1980s' financial fantasy of a free lunch.

To succeed in spurring long-term growth, tax cuts, by and large, must be paid for. But how and at what cost? "Dynamic scoring" is supposed to answer these questions by predicting the effect of tax policy on economic behavior and government revenue. Many supply siders a decade ago used dynamic scoring to estimate that each dollar in tax cuts would create enough economic growth to return a dollar in tax revenues. It didn't work out that way, and taxpayers are still paying the interest on the resulting \$3.1 trillion debt. Without those interest payments, the federal budget would be in surplus. Now, many economists are saying that a buck in tax cuts gets you back 35¢ to 40¢ in tax revenues. Maybe.

Economic research is murky on dynamic scoring. We'd prefer to take a conservative stance and assume that the Treasury could count on only a 30% return at best. That means that 70% of a tax cut must be paid for, dollar for dollar, in spending cuts and higher revenues through closing tax loopholes. A 15% across-the-board tax cut, one idea being discussed in the Dole camp, would transfer \$600 billion over

six years from the government to the people. That's great, but only if the politicians have the courage to find \$420 billion in spending cuts and added revenues from closing loopholes. If not, that's \$420 billion in new deficits, higher interest rates, and lower, not higher, economic growth.

Returning to the simple two-tier income tax system of the sweeping tax reform of 1986 could help. We think getting back to the 15%-to-28% tax rates would shake most of the tax break ornaments out of the tax tree. A simple system that taxes only tax breaks for gasoline, private-purpose bonds (stadiums), and other business and personal activities could generate up to \$50 billion a year. A two-tier tax system would save billions of dollars by simplifying IRS paperwork. Best of all, a two-tier tax system would help stop the recent drift of special-interest tax policies that encourages consumption and distorts more rational economic decision-making. The Contract With America's \$500 billion tax credit, for example, would cost \$147 billion over several years and does virtually nothing to promote economic growth or jobs. Indeed, by promoting consumption, the tax credit also encourages imports and hurts the trade deficit and the dollar.

The goal of a major tax cut must be to foster investment and growth. The U.S. economy is in good shape, and companies are more competitive after years of painful effort. The economy can benefit from lower marginal tax rates, but it can also be hurt by the wrong tax policy. If politicians pander to voters and refuse to pay for tax cuts, they can cause the budget deficit to balloon again, send rates higher, and kill off growth. If they push for tax cuts that boost consumption and not investment, they risk exacerbating the trade deficit, hurting the dollar, pushing rates higher, and killing off growth.

So go ahead and cut taxes. Simplify the code. End loopholes. Lower spending. Focus on investment. But don't blame the gains of a decade.

THINK OF HISTORY, PRESIDENT SUHARTO

Indonesian President Suharto, 75, has plenty to boast about. For the past three decades he has overseen unprecedented growth and prosperity in his nation of 200 million. But now he's facing a crucial—if not historic—juncture. Indonesia's economic success has generated strong pressures for a more liberal, pluralistic society. A rising middle class, labor unions, and the disenfranchised are clamoring for a role in a political system dominated by the military. In South Korea and Taiwan, the same economic and political pressures persuaded the military to step aside in favor of civilian government. If the ex-general can lead his nation into democracy as well as prosperity, his place in history will be equal to that of Indonesia's first President, Sukarno. But if Suharto continues to snuff out opposition, he may leave a legacy of violence and economic decay.

Indonesia's economy is already suffering. The rupiah and stock market are down. And foreign investors, who are financing the country's \$100 billion in debt, are wary. This is particularly true of the overseas Chinese community. Among the targets of the riots were local Chinese businesses.

It's time for Suharto to allow for greater political diversity and create a legal framework for political success. Suharto must also be mindful of those not benefiting from recent economic growth. Cracking down on labor unions trying to raise extremely low wages could fuel resentment and ultimately trigger more rioting. Suharto has a chance to go down in history as a leader with vision if he takes the right moves to allow for greater political expression. It's in everyone's interest for today's economic gains to go up in flames in tomorrow's riots.

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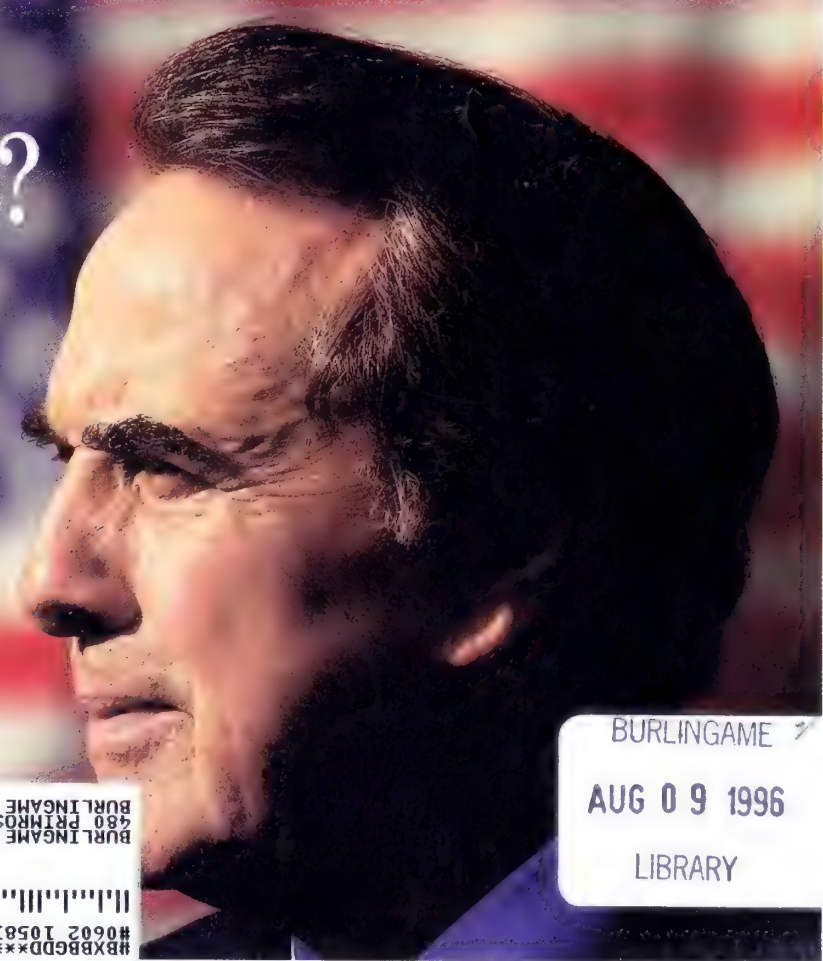
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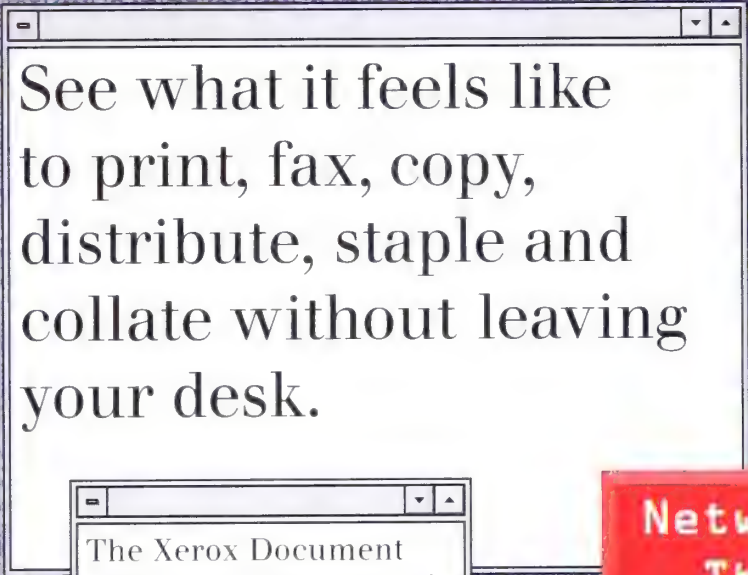
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Good
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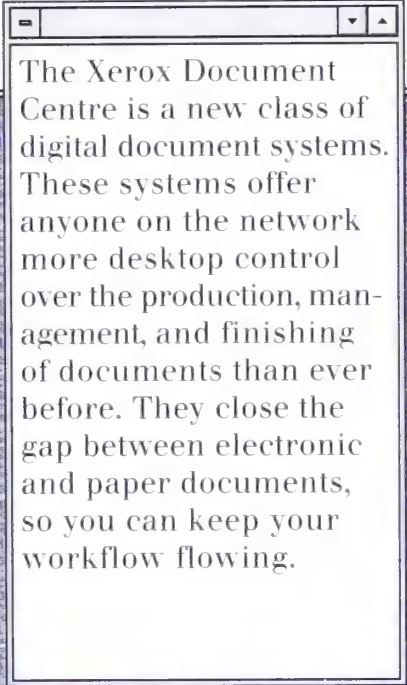


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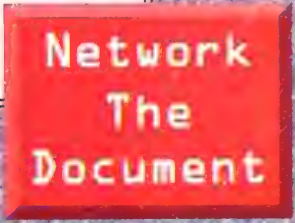
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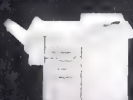
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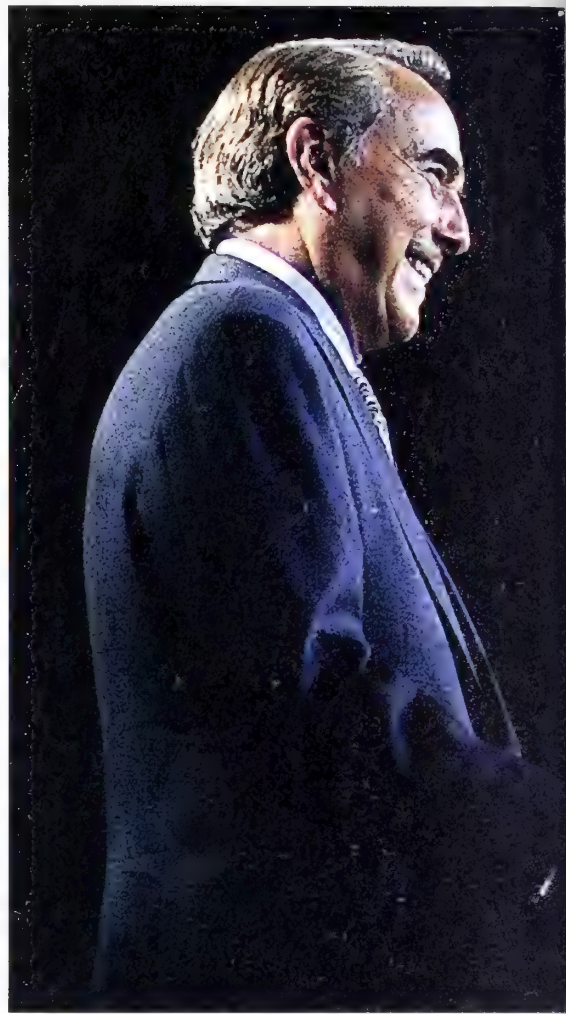
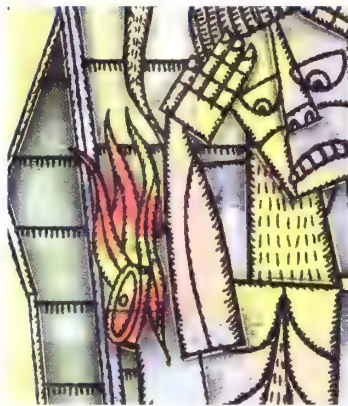
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What led Bob Dole, a balanced-budget man, to propose huge tax cuts offset only by vague plans for spending cuts? Here's the story of the behind-the-scenes squabbling in the GOP camp that led to Dole's dramatic speech. Will the gamble revive his campaign? What might it do for—or to—the economy?

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Finding the money to pay for \$548 billion in tax cuts wouldn't be easy

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EDITED BY LISA SANDERS

CAPITOL OFFENSES

WHO KILLED LOBBY REFORM?

A BID TO SLOW DOWN THE revolving door between Capitol Hill and K Street was quietly killed as Congress adjourned for August. The reform effort, which was led by Senators John McCain (R-Ariz.) and Russell Feingold (D-Wis.), tried to prevent former lawmakers and their senior staff members from quickly cashing in on their expertise by becoming lobbyists.

Currently, congressmen and their aides can't lobby for a year after they leave the Hill. McCain and Feingold would have extended that to two years for former members and five for former aides. The Senate unanimously adopted the measure July 28.

But the provision was axed in a closed-door session between House and Senate negotiators. Nobody claims responsibility, but GOP House

leadership sources say they didn't want to attach it to a routine spending bill. That's exactly what the House tried to do last year to weaken environmental-protection enforcement. Senate conferees stripped that provision from an appropriations bill.

Feingold accuses lobbyists of orchestrating a "classic insiders' job" that killed meaningful reform. He says he hopes to try again by pinning the restrictions to other legislation. *Richard S. Dunham*



FOILED: Feingold and McCain

PRODUCT PEEK

OLIVETTI HEEDS ECHOES OF THE PAST

TRY, TRY AGAIN. THAT'S THE advice Olivetti is taking to heart as it takes another pass at the U.S. computer market. Since 1983, the Italian computer and communications giant has twice jumped in, only to stumble



RESTART: Will the U.S. bite?

and withdraw. Lured now by the hot portables market, it will take one more shot next week with a shipment

of Echos, a line of four Pentium-based notebooks.

Nassir Ahmed, who moved Texas Instruments into the world's top 10 laptop suppliers in five years as its director of worldwide notebook marketing, leads the charge. Now CEO of Austin (Tex.)-based Olivetti Personal Computers USA, Ahmed aims to use relationships with Taiwanese notebook makers and U.S. distributors made at TI to put Olivetti among the top 10 U.S. laptop suppliers by mid-1998. His strategy: To couple aggressive pricing with a focus on small and midsize business customers largely ignored by IBM, Compaq, and Toshiba.

Ambitious? Surely. Aggressive newcomers, such as Hitachi, already have lopped 25% off the price of similar machines. That will force Olivetti to lower the prices on Echos, the cheapest of which has a 100-Mhz chip and was to sell for \$2,499. Analysts Dataquest Europe says similar strategies have helped Olivetti double its Western Europe notebook market share to 4.9% in 1996's first six months. *Gary McWilliams*

NEW WORLD ORDER

POLES SHOP TILL PRICES DROP

THE NOVELTY OF WESTERN consumer goods may be wearing off in Eastern Europe. In Poland, shoppers are getting shrewder than any big Western companies imagined. After the holidays of 1990-91, when locals bought every bottle of H&M olive or box of Pampers available, they're returning to cheaper, and often homegrown, items. More expensive merchandise is reserved for holidays and birthday

To reignite sales, Western companies are developing low-cost alternatives. Germany's Benckiser, for example, compensated for its expensive laundry detergent Lanza, by creating Dosia. A 450-gram box costs 70¢, \$1.30 for Lanza.

The catalyst behind Westerners' strategy is Poland's still-small \$300 a month salaries. In addition,



CHOOSY: Poles prefer value

multinationals must stay competitive with their Polish counterparts' improved marketing and packaging. But Marek Janicki, manager of the Warsaw office of Cann-Erickson Worldwide, sounds a cautionary note. It's not easy, he says, to establish habits adopted during socialism. Even when Poles have the money to buy better products, they may be reluctant. *Peggy Simpson*

THE LIST HEALTH CHECK

Most long-term care patients suffer from impaired intellectual functioning caused by such diseases as Alzheimer's. Almost 80% of

them are in nursing homes for high-level care; the rest are tended to at home. These figures from John Hancock

CARE IS COSTLY

are considered a representative sample by other insurers. Average cost for a year in a nursing home: \$40,000.

LONG-TERM-CARE PATIENTS

AILMENT	SHARE OF INSURANCE CLAIMS
DEMENTIA, ALZHEIMER'S	36%
BONE, JOINT DISEASES	17
CANCER	14
STROKE	13
HEART, BLOOD CONDITIONS	10
ORGAN DISORDERS (STOMACH, LIVER)	4
LUNG DISORDERS	3
WOUNDS, INJURIES	2
DIABETES	1

DATA: JOHN HANCOCK FINANCIAL SERVICES



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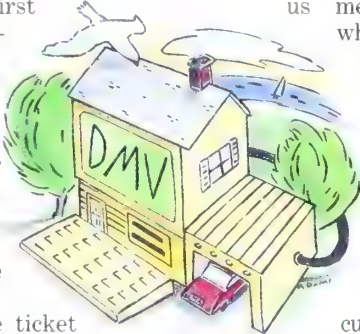
Up Front

I-WAY PATROL

NO WAITING AT THIS DMV

IF YOU GOT CLOCKED DOING 85 mph on the Mass. Pike, now you can pay for it while doing 28,800 bps on the Internet. Massachusetts has become the first state to allow motorists to pay speeding fines and other noncriminal violations via the World Wide Web.

With the ticket number and a credit card at hand, violators surt to the Massachusetts Registry of Motor Vehicles at <http://www.state.ma.us/rmv> and pay for their sins. The Web site, which was developed for \$50,000, also allows motorists to conduct common transactions such as renewing car registrations. More services will become Web-



friendly by fall, including ordering vanity plates.

It's all part of the Bay State's continuing drive to eliminate the endless lines that snarled its offices a few years back—a cause several other states have adopted, although not yet by allowing transactions via the Web. "This will help us meet our goal, which is never to see another customer again," says a spokesman, half-jokingly. Through the Internet service, the state hopes eventually to cut back on some of its \$46 million annual DMV budget.

Cybernauts may feel that Massachusetts still has a thing or two to learn. Department bureaucrats eliminated the use of slashes and periods on plates two years ago, which means that drivers won't be able to get vanity tags to match their Web sites. *Mark Maremont*



LITIGATION NATION

INSURERS HAVE A PET PEEVE

DOGS ARE PUTTING THE BITE on insurers. At State Farm, the largest property-casualty carrier, claim payouts for dog bites are surging—up 15% in 1995, to \$70 million on 11,000 claims. All other pets only cost State Farm \$382,000.

LITTLE NIPPER:

So sue me!

The insurance industry estimates that bites cost it \$1 billion last year.

The actual number of dog-bite claims State Farm processes is growing, too, although less rapidly at a steady 2% annually for the past six years. State Farm pays an average \$6,400 per claim under homeowners' liability policies. Nationally, the Humane Society of the U.S. says up to 3 million dog bites are reported each year. One reason that insurers are paying through the snout: More victims are suing. Also, more households are using canines for protection—twice as many in 1993 as in 1981—and the dogs are often trained to attack. *Susan Jackson*

DRAWN & QUARTERED



HONCHOS

HOW A CHICKEN CHAIN LOST ITS HEAD

JOHN Y. BROWN JR. IS FLYING the coop from his latest chicken venture. Brown, who built Kentucky Fried Chicken into a nationwide chain, has relinquished majority interest in privately held Ken-ny Rogers Roasters, founded in 1991 with the country-western singer. The former Kentucky governor and husband of one-time Miss America Phyllis George (a divorce is pending) will step down this fall as CEO of the 300-plus-store chain.



BROWN balking

Impatient to speed things up, major shareholder Berjaya Group Berhad of Malaysia has upped its in-

vestment steadily in the past three years to assume majority control. (Brown's stake has dropped from 75% to 15%, and people close to deal say he got paid about \$15 million.) Brown will remain as chairman.

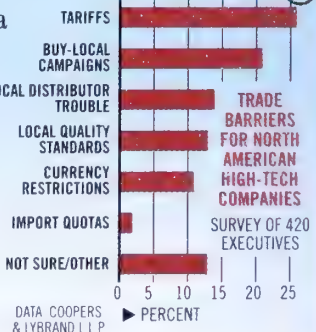
One flash point: timing of a public offering. Brown, who resisted pressure to do it soon, says Roasters' concept needs refinement. The chain had 1995 sales of \$288 million yet isn't profitable.

Rival Boston Market boasts 900 stores and more market clout. Berjaya says IPO capital could move Roasters into that league. *Gail DeGeoe and Ivette Diaz*

THE BIG PICTURE

GLOBAL TRADE WOES

The U.S. and Canada log nearly one-third of high-tech sales abroad. But 99% of execs say trade impediments are a problem. Most, such as quality restrictions favoring local products, are official.



20 THINGS YOU SHOULD DO IN THIS LIFETIME.

- 1) Visit the country your ancestors called home.
- 2) Leave a dollar where a kid will find it.
- 3) Fly over the Grand Canyon in a helicopter.
- 4) Lend money to a friend without expecting it back.
- 5) Have a suit made by a Savile Row tailor.
- 6) Ride in a gondola down the Grand Canal in Venice.
- 7) Teach a class.
- 8) See the sun rise over the ruins at Machu Picchu.
- 9) Plant a tree.
- 10) Fly on the Concorde.
- 11) Stand on the Great Wall.
- 12) Make your own beer.
- 13) See an opera at La Scala in Milan.
- 14) Learn to speak French.
- 15) Take a balloon ride over the Serengeti.
- 16) Be able to recite three good toasts.
- 17) Kiss someone passionately in public.
- 18) Play the Old Course at St. Andrews.
- 19) Shoot the rapids on the Snake River in Idaho.

20)





The new 1997 7-Series

Life is good. Especially when you allow yourself experiences as invigorating as driving a BMW 7-Series. And since it is one of those unique things that can make you feel alive, it seems particularly appropriate that the 7-Series should help you stay that way.

Introducing the BMW 7-Series for 1997.

This year, the BMW 7-Series presents an entirely new level of automotive security and safety, with features ranging from standard side impact airbags and All Season Traction to its exclusive new break resistant Security Glass.

Safety is advanced even further by powerplants that help you to sidestep danger and drive your way out of trouble.

The standard V-8 provided in the 740i and the 740iL boasts the fastest 0-60 time in its class, faster than the far more expensive Mercedes S500. And for those who want still greater control-enhancing performance, there is the 322 horsepower afforded by the 750iL's standard V-12.

Suffice it to say, BMW designed the new 7-Series not just to be a pleasure to drive, but also to be among the safest cars on the road.

Why?

For a reason you only fully grasp when you're strolling through a place like the Musée d'Orsay.

Life is too short already.



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MORE ON NIKE'S OVERSEAS LABOR PAIN

Your story on Nike Inc.'s production practices in Indonesia greatly underestimates the impact of our efforts on behalf of subcontracted workers ("Pangs of conscience," International Business, July 29). The facts are that Nike subcontractors, on a 25-day wage scale, are already paying minimums above \$2.59 and average wages of \$4.76. Meanwhile, factories that shifted to the new 30-day minimum wage took away bonuses to compensate for the increase—bonuses that Nike subcontractors continue to pay for attendance, productivity improvements, and transportation fees, in addition to free meals and medical care.

This compensation is fair. Ongoing, independent audits by Ernst & Young show workers accumulate significant savings. At what the article refers to as the "hell" of Nikomas Gemilang, a December, 1994, audit found 60% of line workers save more than 25% of their monthly pay. In addition, wages have risen 44% since the audit.

David B. Taylor
 Vice-President, Production
 Nike Inc.
 Beaverton, Ore.

ONLY HALF THE STORY ON E-DATA?

The article on E-data Corp. ("E-Commerce: Who owns the rights?" Science & Technology, July 29) says was anything but fair.

You do not include comments made by David Fink, E-data's patent counsel as to "prior art." Fink expressed his opinion of its inapplicability to the actual claims of our patent.

My own background is described in language which constitutes character assassination. I have never been barred from selling stock. In 1975, I pleaded "no contest" to securities laws violations after fighting the charges for over three years. I have never been an investment banker.

The comments about our amnesty

CORRECTIONS & CLARIFICATIONS

Align-Rite International's business was described incorrectly in the table accompanying "Hot growth companies" (Cover Story, May 27). The company makes photomasks used to manufacture integrated circuits.

"Compaq at the 'Crossroads'" (Information Processing, July 22) erred in saying WebConnect Inc. had adopted Compaq Computer Corp. server computers for its Internet service. The story should have cited USWeb Corp. in Santa Clara, Calif.

The article "Run, jump—and sell" (News, Analysis & Commentary, July 29) should have said ESPN broadcasts 17,520 hours of programs per year on its two channels, not 5,300. Also, the company's new channel officially will be called ESPNEWS, not ESPN 3.

In "BUSINESS WEEK's Report on second-quarter earnings" (News: Analysis & Commentary, July 29), earnings estimates for Cascade Communications' should have been adjusted for a stock split. Its estimated earnings-per-share should have been 13¢. Its actual earnings were 17¢, 4¢ more than expectations.

program are misleading. There is nothing in the mailed package that accuses any of its recipients of infringement.

In conclusion, we find it inappropriate for you to publish so biased an article.

Arnold L. Freilich
 President
 E-data Corp.
 Secaucus, N.J.

NOT SO MICRO AT SGS-THOMSON

SGS-Thomson Microelectronics, Europe's largest independent semiconductor producer, appears to have been overlooked in the Global 1000. As of May 31, the survey date, its market capitaliza-

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Readers Report

tion stood at \$5.8 billion, which would place it 550th or so in the **BUSINESS WEEK Global 1000** (July 8).

Pasquale Pistorio
President & CEO
SGS-Thomson Microelectronics Inc.
Saint Genis Pouilly, France

REPORTS OF ITS DEATH ARE GREATLY EXAGGERATED

Your feature on Leon Black ("Wall Street's Dr. No," Finance, July 29) incorrectly refers to E-II Holdings as "formerly American Brands Inc." American Brands did own E-II from February to July, 1988. We purchased several operations from E-II then sold it to a subsidiary of Riklis Family Corp. American Brands Inc. is alive and quite well.

Robert J. Rukeyser
Senior Vice-President
American Brands Inc.
Old Greenwich, Conn.

CHINA AIRLINES HAS CHANGED ITS WAYS

Following a number of troubling incidents a few years ago, China Airlines launched a major overhaul of its safety

management structure ("Dangerous liaisons?" Government, July 29). Performance improved dramatically.

U.S. carriers have chosen to cooperate with China Airlines because they know we are a safe, reliable partner.

Tony T. P. Ting
Vice President, Operations
China Airlines
Taipei

THE TEMPEST OVER TOMATOES

I was disappointed to read your ill-informed attack on James Jones, the U.S. Ambassador to Mexico ("The tomatoes of wrath," Up Front, July 29). Ambassador Jones deserves our compliments for his efforts to mediate a very thorny trade dispute.

American agricultural exports to Mexico increased by 70% in the first quarter of this year. Thousands and thousands of jobs are dependent on these exports, which could be jeopardized by the conflict over winter tomatoes.

I recognize that tomato producers in Florida are having a difficult time. However, if we do not settle this

tomato import problem, under the rules of NAFTA all of agriculture will lose.

Bob Davis
Immediate Past President of the
National Cattlemen's Assn.
Davis, Okla.

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MICHAEL HAMMER BEYOND REENGINEERING

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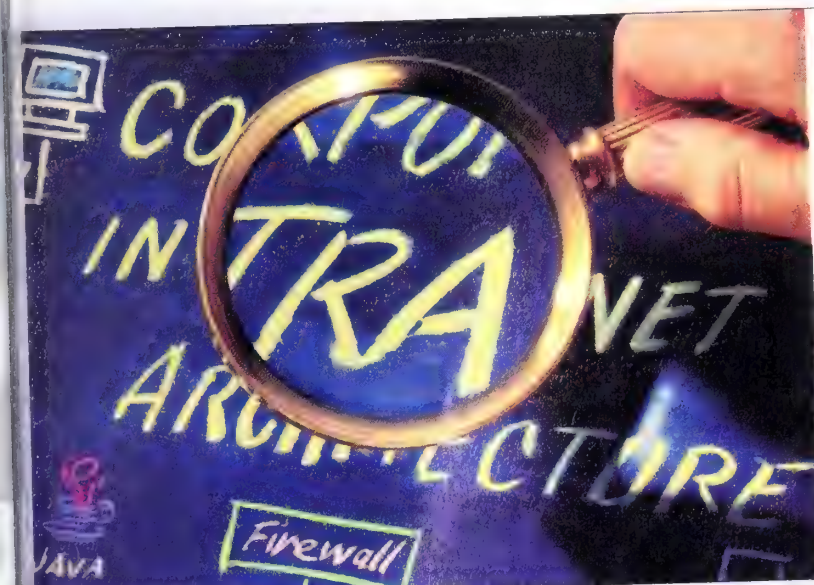
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WHEN WILL THE DEVELOPMENT OF GSM HIT THE WALL? SORRY, BUT WE CAN'T SEE THAT FAR AHEAD.

Does the fact that the Global System for Mobile Telecommunication (GSM) was the world's first digital wireless phone standard mean that it's over the hill? No, in fact, nothing could be further from the truth.

GSM, the basis for new and exciting personal communication services, is poised to go wide-band (64 kb/s). Naturally, this opens the door to a whole world of interesting possibilities.

Surfing the Internet? Certainly. Transferring multi-media files? Definitely. Videoconferencing? Of course, of course, of course. And this rapid expansion in services is matched only by the rapid increase in the number of users.

The GSM user base is growing at the rate of 27,000 new subscribers every day. (Little wonder then, that there are already over 16

million subscribers worldwide.) But more importantly, GSM is technologically equipped to handle this huge wireless market. A GSM network can grow almost endlessly even in the busiest and most congested areas.

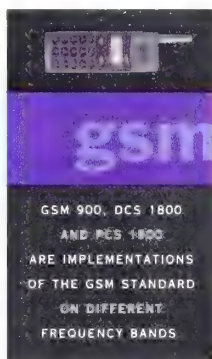
However, these aren't the only reasons why operators prefer GSM to standards that are as yet in their infancy.

With GSM networks in operation in well over 60 countries, the potential for global roaming is obviously, enormous.

And with over 800 international roaming agreements already in place, the present is just as attractive as the future.

So then, where does all this leave certain newer standards that are as yet barely operational?

Sorry, but we can't see that far behind.



GSM. The standard that sets the standard.

ERICSSON 

BEYOND REENGINEERING

How the Process-Centered Organization Is Changing Our Work and Our Lives

By Michael Hammer

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REENGINEERING RECYCLED

These are tough days for businesspeople. Profits are hard to come by, and the pace of technological change seems to make planning futile. So it's not surprising that CEOs everywhere turn in desperation to consultants for advice. Unfortunately, many executives end up bewildered. One consultant recommends a dose of reengineering, another points to a tight focus on core competences, yet another favors boosting economic value-added, and so on.

Now, add to the list a pitch to become "process-centered." That's the quality that characterizes the 21st-century corporation, according to consultant Michael Hammer's latest how-to, *Beyond Reengineering*. Hammer, who, along with his former partner James Champy, helped spawn the reengineering movement, once again tries to inspire nervous businesspeople to embrace change. His recipe? "The radical redesign of business processes for dramatic improvement."

But isn't this just plain old reengineering? No, says Hammer: It is the same definition he has always used for reengineering. But previously, he says, "I felt that the most important word in the definition was 'radical.'" Today, he realizes, "the key word... is 'process': a complete end-to-end set of activities that together create value for the customer."

Changing the word emphasis hardly amounts to a huge revelation. Hammer's incremental shift pales next to the critique his former colleague leveled at reengineering almost two years ago. In the 1994 book, *Reengineering Management*, Champy renounced reengineering's overemphasis on impersonal processes, instead extolling management leadership. But one hardly expects Hammer, an engineer by training, to take such a warm and fuzzy approach.

So what we have here is a restatement of first principles. *Beyond Reengi-*

neering is useful as far as it goes, peppered with smart insights about what it takes to make it in business these days. But Hammer's unwillingness to address the human side of corporate change—so much in the news over the past few years, thanks to downsizing—gives the book a bloodless feel. There's passion aplenty here about the need to change, but no warmth. He lectures that the New Business Order will free people to use their brains at work and take on bigger responsibilities, then admits "the engineer may find himself working at full steam all day, all week, all year." He adds: "Many forty-four-year-olds will find it exhausting."

In Hammer's world, that's just the way it goes. You'll be tired, but at least, Hammer says, your job will be more rewarding. Why? You can thank process centering. Hammer never provides a neat definition of what the term means. His first stab is fairly tautological: "Process centering," he writes, "more than anything else, means that people—all people—in the company recognize and focus on their processes."

Reading on, it becomes clear that process centering means reuniting the various parts of such now-fragmented functions as customer service so that customers actually get served rather than just passed from one worker to another. At GTE Corp., for example, each customer-service worker was once limited to performing a single task—diagnosing a technical problem, say. Now, they are involved with the full range of work required to resolve a snafu. This means GTE's "customer care advocate" must be a master of several disciplines, ranging from assessing problems to dispatching technicians to dealing di-

rectly with customers. The result, Hammer says, is that 33% of problems are resolved on a customer's first call.

The better part of this book is spelling out the implications of becoming process-centered. Each worker transforms him or herself into a professional, "someone who is responsible for achieving a result rather than performing a task," he writes. "A worker is kind of organic robot, operated by manager via remote control." Professionals, on the other hand, possess "whole jobs," where they act and think for themselves. Meanwhile, companies will have to destroy the walls erected between them and their suppliers, that they form "a kind of corporate consortium, each member contributing special expertise."

If you've stayed current with the latest management theories, none of this will seem particularly new. It's all well-stated, if a bit naive. For instance, it lauds customer relations at General El-

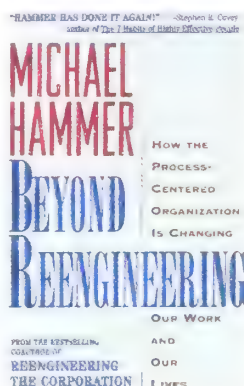
tric Co.'s Large Appliances Div., but later in the same chapter, when he talks about supplier relations, he fails to note that the division has consistently treated suppliers poorly, demanding they cut prices or lose business. So much for partnership.

The book's most useful new insight is that processes, not products, might provide companies with a new form of competitive advantage. Like L. L. Bean Inc., which has broken new ground by selling its order-taking service to the likes of AT&T, he suggests that companies might sell their processes rather than rushing into new fields or just concentrating on current products.

Unfortunately, there isn't much else that's new here. *Beyond Reengineering* is a rather dry book that does a good job of explaining the challenges businesses face—but does little to ease executives' confusion regarding how to move forward. Perhaps Hammer's overprocess, which has created three reengineering books in four years, could stand some reexamination.

BY KEVIN KELLY

Former *BUSINESS WEEK* correspondent Kelly now runs a small manufacturing company in Union City, Calif.



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BY THANE PETERSON

CEZANNE & CO. ON CD-ROM

From the Louvre to a lecture on Van Gogh, new CD-ROMs offer a rich experience in art

It used to be you had to load up on bulky books to see art reproductions. But lately CD-ROMs have emerged as a good alternative. The best of the new art CD-ROMs pop into either a PC or Macintosh and start right up. Before you know it, you're cyberstrolling down digital museum halls and stopping to look at paintings. You can home in on details with a "magnifying glass" and read about the work, the artist, and related themes. CD-ROM reproductions are less detailed than those in the best art books, and they're certainly no substitute for seeing the originals. But they're a good way to get to know artists and their works before heading to a museum or gallery.

Some of the very best new art disks have been produced by Corbis, which was started by Microsoft's William H. Gates III. For instance, if hearing about the landmark Cézanne exhibit at the Philadelphia Museum of Art has piqued your interest, you'll want to check out Corbis' marvelous new CD-ROM on the painter's career and works. I plugged it in at 11 o'clock one evening for a quick look and was so fas-

cinated that two hours went by before I knew it.

The disk is packed with information, not just about Paul Cézanne's paintings but also his life, contemporaries, and artistic antecedents. You can start out looking at the paintings, either by taking a digital "tour" or by choosing them by name from an index. And as you click on links to related subjects, you may end up reading about anything from the novelist Emile Zola

impressionist art near Philadelphia, is equally well done (it comes in separate Macintosh and PC versions). Corbis plans to release a new disk later this year on Leonardo da Vinci.

Another company putting out some beautiful products is Voyager, based in New York's SoHo art district. *Van Gogh: Starry Night* is a lecture by University of California at Los Angeles art history professor Albert D. Boime that takes as its point of departure Vincent van Gogh's famous painting of the night sky at Saint-Rémy, France. Boime's main point is that van Gogh, who was in an asylum in 1889 when he painted the work, was far from the "mad" artist of legend. Rather, by showing everything from selections of

tute of Chicago is a disk kids about the famed museum. It features wacky icons (you click on giant red letters to hear a gloss on each artwork) and sound effects. The Voyager disks are hybrids that run on Macs and PCs with Windows.

HUGE COLLECTION. It does take a special exhibit or special effects to make a CD-ROM rewarding. *Le Louvre*, a new disk from BMG Interactive Entertainment, is an example. The Louvre's huge collection can be daunting to visit, but the CD-ROM helps narrow things down. The historical and aesthetic analysis of paintings are quite good and you can click on museum maps to locate the ones you don't want to miss. For instance, I've seen *The Caricature of the Ace of Diamonds*, a 16th-century painting by Georges de La Tour, at the museum but never knew much about it. The disk told me where to find it again and explained the painting's unusual lighting and the allegorical meaning of the card game depicted. Voyager also has a Louvre CD-ROM for kids.

Another renowned museum with myriads of treasures is the Hermitage in St. Petersburg, Russia. *The Hermitage Art Treasure Tour* from Cascade Marketing International (509 664-0322, \$49.95), is less polished than the others and doesn't run on Macs, plus I found it confusing to use. But getting a glimpse of the Hermitage's extraordinary antiquities and well-known paintings was worth the trouble. The disk can be viewed in English or Russian. With all the great museums around the world, there should soon be an art CD-ROM for every taste.



LE LOUVRE

The Palace and Its Paintings (BMG Interactive, 800 221-8180, \$49.95) A room-by-room tour of the art and architecture of one of the world's great museums.

PAUL CEZANNE

Portrait of My World (Corbis, 800 246-2065, \$45-\$55) Traces the life of and influences on the great Impressionist, whose work is now the subject of a major retrospective at the Philadelphia Museum of Art.

VAN GOGH

Starry Night (Voyager, 800 446-2001, \$39.95) A detailed history and analysis of a famous night-sky scene the artist painted while committed to an asylum.

A PASSION FOR ART

Renoir, Cézanne, Matisse and Dr. Barnes (Corbis, 800 246-2065, \$40-\$45) Another room-by-room tour, this one of the Impressionist and Post-impressionist collection at the Barnes Foundation near Philadelphia.

(a school pal of Cézanne's) to the birth of photography and its effects on painting. In checking out influences on Cézanne, I discovered some wonderful Pissarro landscapes and a Goya self-portrait I didn't know about.

NOW, VOYAGER. The graphics on the disk are imaginative, and the hybrid product worked with few glitches on both a Macintosh and a PC running Windows 95. *A Passion for Art*, a Corbis CD-ROM about the Barnes Collection of Impressionist and Post-

the artist's letters to astro-nomic analyses of his starry night depictions, Boime argues that van Gogh was a disciplined craftsman with a lot of down-to-earth good sense.

Painters Painting, another Voyager product, is partly based on a documentary film about such New York School artists as Barnett Newman, Jackson Pollock, and Willem de Kooning and traces the school's development from the 1940s on. *With Open Eyes: Images from the Art Insti-*

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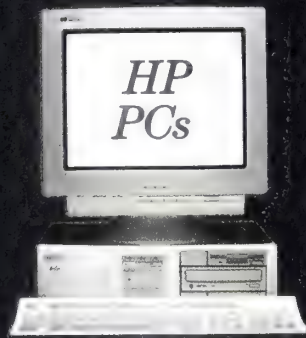
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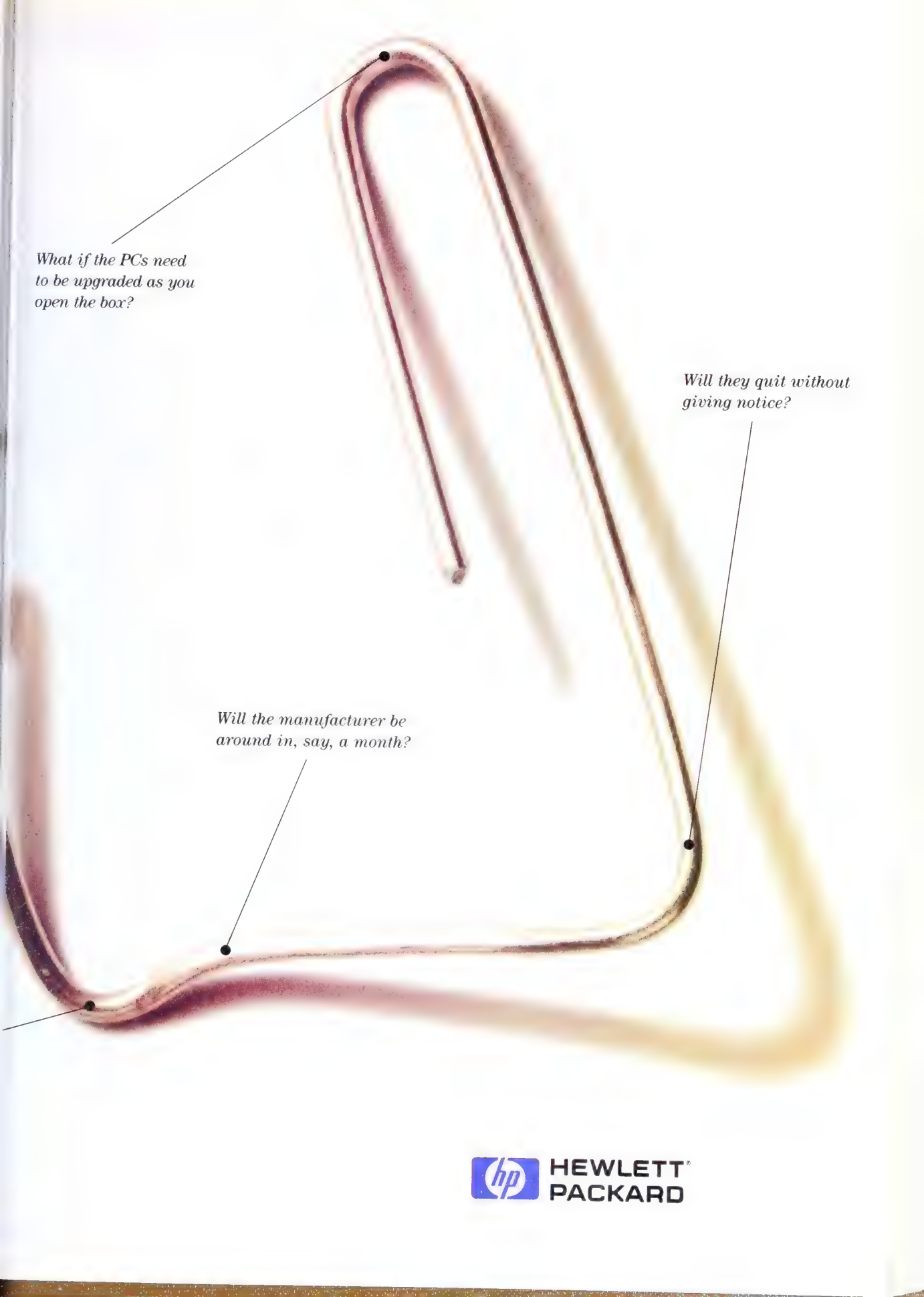
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*What if the PCs need
to be upgraded as you
open the box?*

*Will they quit without
giving notice?*

*Will the manufacturer be
around in, say, a month?*

BY PAUL CRAIG ROBERTS

BOB DOLE'S BABY STEPS TOWARD THE SUPPLY SIDE



NEW MOOD:
His 15%
tax-cut plan is
barely enough
to satisfy
Reaganites.
But with this
more hopeful
message, Dole
may have a
chance to win

Bob Dole—a tax-cutter? I write about this with great trepidation. The chances are high that before this column goes to print, Dole will have flip-flopped again, declaring his opposition to “irresponsible tax cuts.” After all, he has abandoned his own Dole-Canady bill, which would eliminate race and gender quotas in the federal government; trashed his promise to repeal the Clinton ban on selected guns; and backburned his pro-life stand on abortion, all in the name of political expediency.

This same expediency has now brought Dole to tax cuts. What he will find out is that choosing the easy path does not bring enough commitment to face down either the Democrats’ (and the media’s) class-warfare rhetoric or the Republican Establishment’s deficit doom. By leading with a policy he doesn’t truly believe in, Dole risks emphasizing his worst trait.

Still, I can’t help crowing a bit that Dole had to turn to the supply side in order to revive his failing Presidential campaign. Dole is no doubt hoping that some of supply side’s optimistic aura will attach to him. When supply side entered the fray 20 years ago, the country was certainly in a dark mood. President Carter was talking about “malaise,” and stagflation seemed to doom our future. Supply-side economists revived hope by showing that rising inflation and unemployment were not an inherent feature of our economy but the product of an incorrect policy mix that could be changed. And it was. No one has seen stagflation since President Reagan cut tax rates and abandoned the policy of trying to inflate the economy to prosperity.

THE NANNY STATE. Politicians who appeal to the optimistic streak in the American character do well. No amount of denigration can hide the fact that Ronald Reagan is the envy of every politician. Dole is right to want to shed his dour image for an optimistic one.

If Dole can stick with his new face long enough, he has a chance. The nanny state has proved to be less successful than the Reagan economy. A measured step away from government entitlements toward individual wealth and responsibility is a proper political program. This is especially true with demographics turning against intergenerational-transfer programs such as Social Security and Medicare.

Would Dole’s supply-side program work or just deliver a setback to deficit reduction? The plan’s boost to incentives is small, compared

with the 1981 tax cut, but other conditions are more favorable. Cutting federal expenditures is not as controversial as it was 15 years ago, and inflation is no longer raging. That means the Fed is unlikely to panic and run the budget deficit with tight money, as it did in the 1980s. (The “Reagan deficits” resulted from a more-rapid-than-expected collapse of inflation that caused nominal gross national product and tax revenues to be less than forecast.)

FLAT-TAX COMPLICATIONS. Still, Dole’s tax cut is barely aggressive enough to garner supply-side support. The 15% reduction in tax rates would bring the top rate down from 34% to 28%, but leave it higher than Reagan’s 28%. The middle rate would fall from 28% to 24%, and the bottom rate from 15% to 12% or 13%. The incentive effect from the rate cuts in the lower brackets would be positive but not substantial.

The halving of the capital-gains tax from 28% to 14% would noticeably cut the existing tax bias against saving and investment and spur entrepreneurial activity. The expansion of individual retirement accounts would also reduce the tax bias against saving, and the repeal of Clinton’s tax hike on Social Security benefits would be a nice step back from the evolution of Social Security into a means-tested welfare system to which all Americans contribute but from which only the poor collect.

Dole’s tax-rate reductions, however, could complicate more basic reforms, such as a flat tax. Unless government’s size is cut further, it is unlikely that a flat tax as low as 12% or 13% can be implemented. That would saddle flat-tax advocates with the hard sell of a flat rate that would raise the income tax rate on the poor.

Another potential problem comes from the \$500-per-child tax credit. It suggests that Dole thinks families are not helped by tax rate reductions or that they are helped more by credits. This undermines the supply-side incentive approach. Why not give everyone a credit instead of lower tax rates? Moreover, does Dole really think that he can open a tax bill to one organized interest group without others demanding tax breaks, too?

The income tax discourages work and investment and supports a welfare system that encourages sloth. If we are going to be stronger, more self-reliant people, we must have a tax system that enables us to look after ourselves. Two cheers to political expediency for bringing this home to Bob Dole.

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Economic Trends

BY GENE KORETZ

A MUTUAL-FUND SELLING PANIC?

Why it isn't on the horizon

Wall Street's current nightmare is that the huge rush into mutual funds in recent years could suddenly turn into a reverse stampede—bringing the long bull market that began in the early 1980s to a traumatic end. For now, however, economist Martin Barnes of *The Bank Credit Analyst* is dubious.

To be sure, the flow of cash into domestic stock funds has already abated sharply. With mutual-fund cash reserves at a historically low level, any surge out of funds could trigger a major market sell-off. And the fact that inflows to equity funds in the first half of this year exceeded total household savings doesn't help matters.

But all of that, Barnes believes, simply suggests that a slowdown in fund purchases was more or less inevitable. The real question is whether the current risk profile of households and the psychological and economic factors influencing their

baby boomers—suggests that purchasers increasingly view their holdings as long-term investments. And equity funds experienced only very brief periods of net redemptions during the market corrections of 1987 and 1990.

Barnes concludes that while a further market correction undoubtedly lies ahead, a massive sell-off of equity funds is likely to occur, if at all, only in the wake of a crushing bear market. And the economic developments that could spark such a bear market—such as a severe recession or major inflationary buildup—are still nowhere in sight.

LOW TECH MAY NOT MEAN LOW PAY

Pencil pushers vs. computer users

Is the wide gap that has opened between the wages of skilled and unskilled workers in the U.S. and other countries over the past 15 years mainly the result of technological change or of such factors as declining unionization, import competition from low-wage countries, and a falling minimum wage?

Noting the growing use of computers, most economists think the cause is "skill-biased" technological change. And they often cite as evidence a landmark study by economist Alan Krueger of Princeton University that found that U.S. workers using computers earn 10% to 15% more than their peers.

Now, however, economists John E. DiNardo of the University of California at Irvine and Jörn-Steffen Pischke at Massachusetts Institute of Technology have come up with intriguing results from an analysis of similar data covering German workers. Predictably, they found that computer usage increased markedly from 1979 to 1991. They also found that German workers using computers enjoy wage premiums similar to their U.S. counterparts.

It's their added findings that are surprising. Unlike the U.S. data, the German surveys included information on workers' usage of pencils, telephones, and calculators. The researchers found that German workers using such low-tech items enjoyed wage premiums almost as high as those using computers.

Such results, of course, don't mean that technological change isn't behind widening wage gaps, though they may provide ammunition to those who think its role has been exaggerated. But they do suggest that rising computer usage itself may be far from the whole story.

GAINS WITHOUT INFLATION PAINS

Bottlenecks are less of a threat

Although industrial production was up nearly 6% in the second quarter, capacity utilization rose just 0.6% between March and June. All of which leads economist Carl Palash of Money/Watch, a market advisory service, to predict that further output gains are unlikely to run into bottlenecks or related price increases anytime soon.

The explanation, of course, is the rapid growth of industrial capacity. As far in 1996, notes Palash, capacity has been expanding at a healthy 4% annual pace, up from 3.8% last year, 3.6% in 1994, and just 2.1% as recently as 1992 and 1991. "Along with continuing labor passivity," he says, "strong capacity growth suggests that the economy can grow faster than in the past without sparking inflation."

A SLIGHT FROST ON GLOBAL DEALS

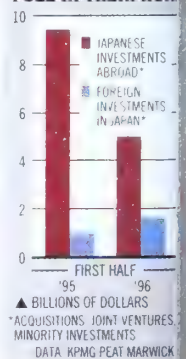
Crossborder mergers decline

The pace of crossborder mergers and acquisitions, which has been setting records in recent years, appears to be topping out. KPMG Peat Marwick reports that the value of global deals in the first half of 1996 fell to \$110.5 billion, below the year-earlier level, while the number of deals declined by 12%.

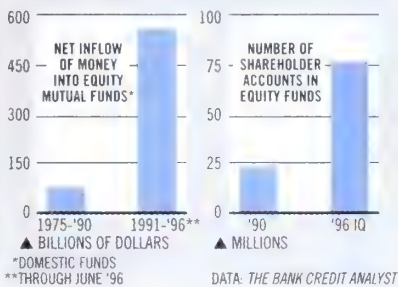
While the U.S. led the pack in both purchases and sales, the value of its purchases abroad and sales to foreign companies both dropped by between \$4 billion and \$5 billion. Britain was next among industrial nations attracting mergers and crossborder funds, racking up a 30% increase, to \$18.7 billion, while raising its own outlays overseas by 21%.

The biggest surprise: Foreign purchases by Japanese companies fell by 47%, to \$5 billion. Possible reasons include Japan's declining current account surplus and worries about the sustainability of the current recovery.

JAPAN'S DEALMAKERS PULL IN THEIR HORNS



THE STAMPEDE INTO MUTUAL FUNDS



investment behavior suggest the possibility of a near-term catastrophic mass liquidation of equity mutual funds. And here the evidence seems reassuring.

For one thing, Barnes observes that despite the mutual-fund explosion, directly owned equity funds account for only 3 1/4% or so of household financial assets—and a still surprisingly low 5 1/4% when funds held indirectly, via pension plans and trusts, are included.

Other positive omens: Many fund holders are still sitting on sizable gains from recent years and are likely to downplay market turmoil as long as they are ahead of the game. The rapidly rising share of mutual-fund assets in retirement plans—and the aging of the

JAMES C. COOPER & KATHLEEN MADIGAN

ENJOY THE SUMMER, THEN START WORRYING AGAIN

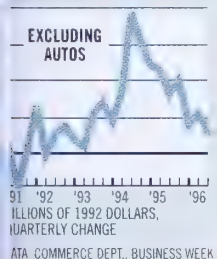
rate hike is unlikely now, but growth could bring back inflation jitters

U.S. ECONOMY

Wall Street dodged a bullet. The financial markets had eked down, anxiously awaiting the crucial early August volley of data that would determine whether or not the Federal Reserve would hike interest rates at its Aug. 20 meeting. As one report after the other came in, either near or below expectations, bond prices took flight like a rocket and stocks zoomed close behind, as the markets surmised that the chances of a rate increase sometime soon had dropped sharply.

What does this onslaught of data on everything from wages to gross domestic product say about the outlook? Most important, as the stock and bond rallies waned, the numbers did not "persuasively suggest an intensification of oncoming inflationary pressures." That's the succinct Fed speak direct from Chairman Alan Greenspan, cribbing the criterion for Fed tightening.

INVENTORY GROWTH HAS SLOWED SHARPLY



More recently, the Fed's beige book, a roundup of economic activity in the Fed's 12 districts, reported that economic growth had "moderated" in some regions and that "wage pressures remained subdued." With rate-hike worries aside, the yield on the benchmark 30-year Treasury bond dropped to 6.75% on Aug. 6, from 7.10% before the latest data came out. And the Dow Jones industrial average broke through 5700 again on Aug. 7, wiping out all of the losses incurred during the steep July correction. The bond market so far remains undistracted by the potential impact on the credit of Presidential hopeful Bob Dole's tax-cut plan, but it's a factor that bears watching (page 28).

THIS DOESN'T MEAN, however, that the markets—or the Fed—are off the hook indefinitely. The latest data also does not suggest that the economy is slowing to a pace that would prevent inflation fears from resurfacing later on. To be sure, third-quarter growth is unlikely to match the second quarter's 4.2% surge in real GDP, the fastest pace in two years. But even though July's data looks soft in places, the evidence that growth is slipping below 3% is far from compelling.

The breakdown of second-quarter GDP shows one

reason. Final demand by consumers, businesses, government, and foreigners rose at an annual rate of 3.5% last quarter, even faster than the first quarter's 3% pace. At the same time, inventory growth, outside of the auto industry, has slowed (chart). Excluding the strike-related ups and downs of auto inventories, second-quarter stockpiles grew at the slowest rate in three years. Heading into the second half, inventories are very lean relative to demand, a condition that will generate additional ordering and output.

That's why the sudden weakening in the July report from the National Association of Purchasing Management may not be a true reflection of the industrial sector. The NAPM's index of industrial activity fell sharply last month, to 50.2%, from 54.3% in June.

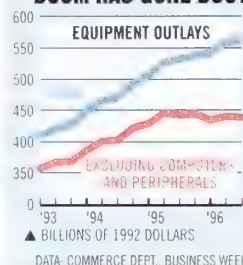
The index may have looked weaker because the seasonal adjustment process may not be capturing the increasingly early summer shutdowns in the auto industry, as carmakers retool for the 1997 model year. That effect is already known to have distorted the data on new jobless claims and the Chicago area purchasing managers' report.

The drop in the NAPM's index was a major factor in the markets' rally, but it will take the August index to confirm whether the July decline was real or just a head fake. The Fed's beige book noted that manufacturing showed signs of accelerating, with factory hiring on the rise in many regions.

THE OUTLOOK FOR SPENDING, meanwhile, remains firm. In the second quarter, demand got its strength from faster growth in the consumer, housing, government, and export sectors, while the drags were in imports and slower capital investment. More imports, though, are just a reflection of strong U.S. demand.

On the surface, the slowdown in capital spending is a little more troubling, given its huge contribution to this expansion. The downshift is centered in traditional low-tech sectors (chart), such as transportation equipment and industrial machinery, while outlays for computers and peripheral items are still booming, helping to lift the total. Looking ahead, though, capital spending will get new support from this year's pickup in the

WHERE THE INVESTMENT BOOM HAS GONE BUST



Business Outlook

economy, along with good, although slower, profit growth, rising capacity utilization, and the continued low cost of capital.

At the same time, the other sources of demand show no signs of falling out of bed. In particular, exports may even speed up, given Europe's new momentum, Japan's firmer footing, Canada's improvement, and Mexico's recovery. And the consumer sector should remain solid, given good job growth and bigger pay gains amid tight labor markets.

WITHOUT A DOUBT, consumers have been the year's biggest surprise. Their spending rose a stout 3.7% last quarter, a shade faster than the first quarter's 3.5% pace. That's the strongest two-quarter advance in 3½ years.

Third-quarter spending appears to have started slowly. Sales of domestic and imported cars and trucks in July fell to an annual rate of 14.3 million, from June's 15.2-million rate, which was also the average for the second quarter. Also, retail surveys reveal softer department-store sales, although analysts say the distraction of the Olympics coverage, especially on weekends, cut into sales, both in stores and on car lots.

Now that all the gold medals are packed away, consumer spending should show more gusto. That's because consumers started the third quarter with more confidence and money, and you don't have to look

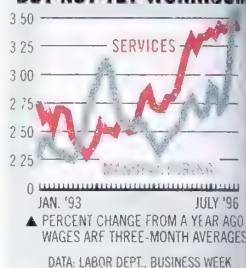
much beyond the labor markets to see why.

Payrolls, after increases averaging 237,000 new jobs a month during the first half, rose 193,000 in July. That's a pace that will keep the unemployment rate at July's tight 5.4%—or heading lower. And it will allow wages to grow at a faster clip. Although hourly earnings in July dipped 0.2% after surging 0.8% in June, the trend in wage growth remains up for both manufacturing and services (chart).

The Fed will be watching that potentially inflationary trend closely in coming months, but pay hikes will also provide healthy gains in consumer incomes. Personal income advanced a sturdy 0.9% in June, the largest monthly increase in a year and a half. And the rally in the markets will support both consumer spending and housing, as fixed mortgage rates will be heading down.

For now, at least, Wall Street has put aside its fears of overly strong growth, rising inflation, and Fed tightening. But until the economy shows clearer signs that it is slowing to a pace that will keep the Fed on the sidelines, the markets could still get hit by shrapnel from any unexpectedly strong data.

WAGE GROWTH: FASTER BUT NOT YET WORRISOME



BRITAIN

WILL LONDON RATES COME FALLING DOWN?

Strong consumer spending had been reducing the chances for an interest-rate cut in Britain. But the continued signs of an ailing factory sector have meant that a cut is not out of the question.

Industrial production fell unexpectedly in June, by 1.1%, with manufacturing down 0.3%. Over the past year, total output is up 0.8%—the slowest rate in more than three years. The sluggishness is also reflected in the Confederation of British Industry's manufacturing survey. Executives are upbeat about output increases, but weak export performance is causing pessimism about orders (chart).

Optimism about output suggests

that excess inventories finally have been cut. In fact, a large drop in stockpiles of finished goods was a reason for the decline in July's purchasing managers' index to 50.7%, from 51.8% in June.

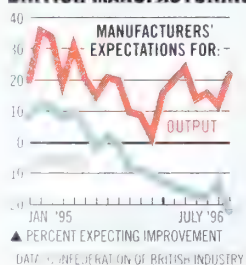
Consumer demand, meanwhile, is solid, as shown by strong retail reports, a healthy housing market, and rising confidence. Still, the inventory adjustment and the fallout from mad cow disease hurt second-quarter real gross domestic product: It grew by 0.4%, or 1.8% from a year ago. That's the slowest pace in three years, and well below the government's target of 2.5% for 1996.

Manufacturing's ills could give Chancellor of the Exchequer Ken-

neth Clarke an opening to ease up. He cited the industry's problems when he cut the base lending rate to 5.75% on June 6, the third cut this year. Rates were left unchanged at the July 30 meeting between Clarke and Bank of England Governor Eddie George. And George is sure to oppose a rate cut at their upcoming Sept. 4 powwow. George is likely to point to the Aug. 7 BOE inflation report that said rates must increase if underlying inflation, which excludes mortgage interest, is to fall to the government's target of 2.5% from 2.8% now.

For Clarke, though, the window of opportunity is closing. The ruling Conservative Party must call elections by May 1997. That means rates would have to fall soon if voters are to enjoy stronger growth by next spring.

A MIXED OUTLOOK FOR BRITISH MANUFACTURING



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If you're a business that sends lots of packages every year, you could save a lot of money with Priority Mail™ from the U.S. Postal Service. Priority Mail two-pound two-to-three day packages are only \$3. FedEx® two-day service is about \$12 and UPS® about \$6.* That adds up.

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\$12



\$6



\$3

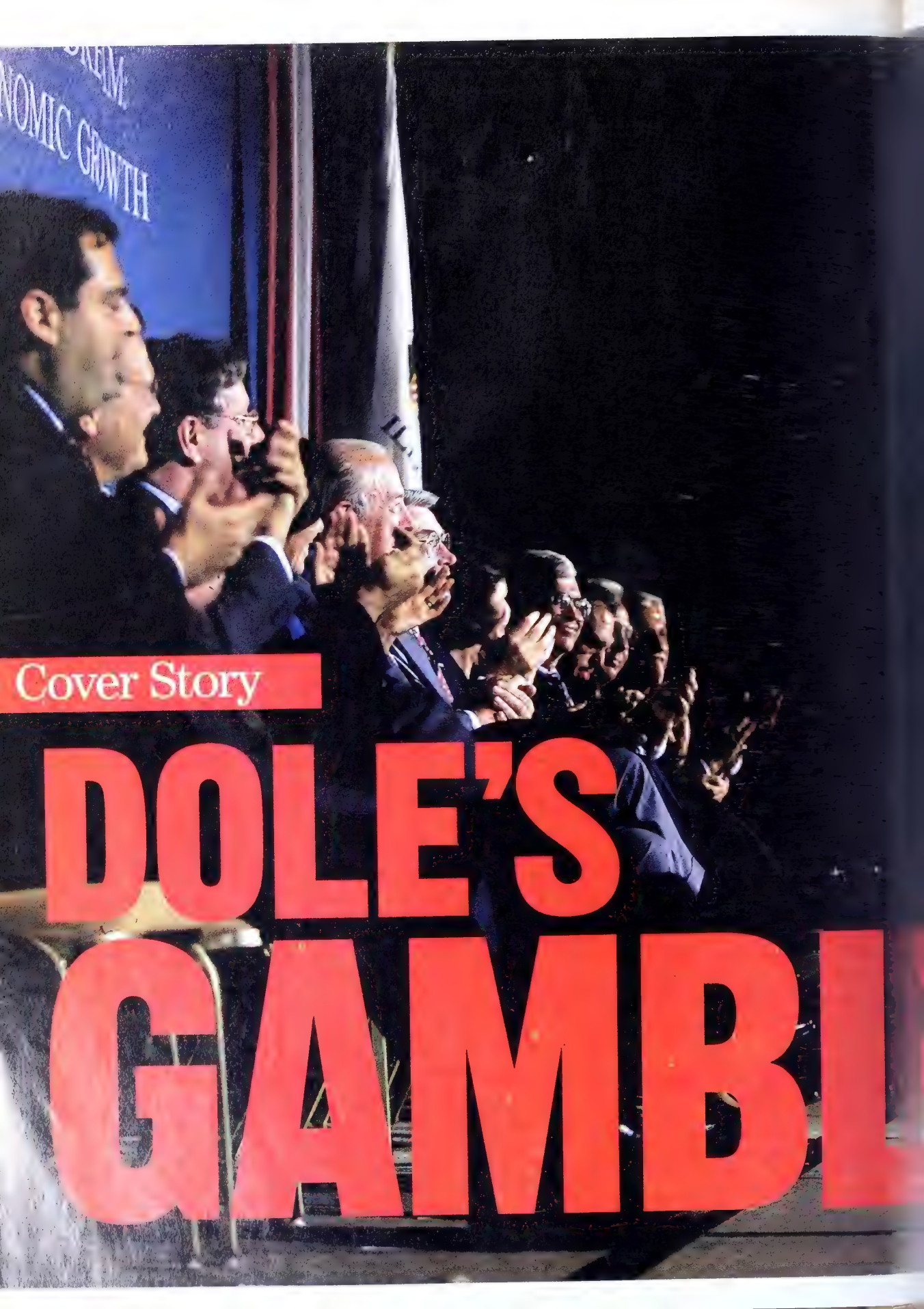
What's Your Priority? <---



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Cover Story

DOLE'S GAMBLE

Why he took the leap, and how he and his brain trust hammered out a dramatic proposal

Munching pizza at his campaign headquarters on the night of July 11, GOP nominee-in-waiting Bob Dole subjected his economic advisers to a 2½-hour grilling. Under mounting pressure to ignite his sputtering campaign with a dramatic economic plan, Dole had already signed off on a \$500 billion-plus tax cut. But he had dithered for two months on specifics. Now, with the convention a month away, Dole had to figure out which taxes to cut and how much growth the cuts would produce.

Two competing camps of advisers—supply siders, led by publisher Steve Forbes, and traditional economists, led by University of Chicago Nobel Laureate and BUSINESS WEEK columnist Gary S. Becker—were locked in debate. Supply siders believed that huge tax cuts would generate so much growth that new revenues would offset up to 50% of the cost. Traditionalists argued that even a program pairing tax reduction

with regulatory reform and education and training incentives would only recapture 30% of the cuts—even- tually. More than \$100 billion in gut-wrenching spending reductions would ride on Dole's choice.

Behind these economic arguments lurked a vital political question: How could Bob Dole, lifelong budget-balancer and deficit hawk, credibly adopt an economic plan built on big tax cuts offset by vague and dubious spending cuts?

Ever the pragmatist, Dole decided to keep one foot in both camps that night: He adopted supply-side economics without fully accepting its tenets. That instinct

to split the differences has led Dole to a program that pins hopes for stronger growth on both tax cuts and such Re-

ELECTION '96

THE TAX CUTS

\$548 BILLION

THE GROWTH DIVIDEND

\$147 BILLION

THE SPENDING CUTS

\$217 BILLION

GROWTH IN NATIONAL DEBT

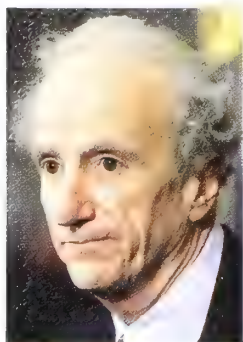
\$184 BILLION*

PLAN OVER 10 YEARS. *PRIMARILY UNDEVELOPED.
DATA: BOB DOLE FOR PRESIDENT CAMPAIGN, BW

PARTY PLEASER

Dole's economic package bears the stamp of his many advisers and gives a break to every faction of the Republican Party

GROWTH ECONOMISTS



GARY BECKER
JOHN TAYLOR

- ▶ 15% across-the-board income-tax cut for all Americans
- ▶ Job-training vouchers
- ▶ Savings incentives

SUPPLY SIDERS



STEVE FORBES
JACK KEMP
JUDY SHELTON

- ▶ Rollback of 1993 tax hike on Social Security benefits
- ▶ 50% cut in capital-gains tax rate, to 14%

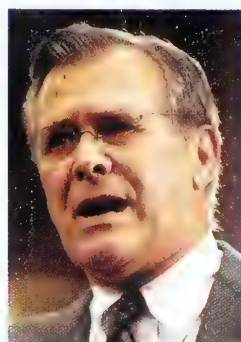
DEFICIT HAWKS



SEN. PETE DOMENICI

- ▶ Pledge to call for balanced-budget amendment
- ▶ Promise to balance the budget by 2002
- ▶ Three-year phase-in of tax cuts

CORPORATE CHIEFTAINS



DONALD RUMSFELD

- ▶ Regulatory reform to subject new regulations to a cost/benefit analysis
- ▶ Legal reforms to rein in product-liability lawsuits

SOCIAL CONSERVATIVES



RALPH REED
BILL BENNETT

- ▶ \$500-per-child tax credit
- ▶ Education vouchers for private- or public-school tuition

publican orthodoxy as deregulation, budget balancing, and education reform. Dole's economists convinced him that with this eclectic mix, he can return America to its economic golden age, lifting growth from the current annual rate of 2.3% to a sustainable 3.5% pace by 2002. "We must commit ourselves to a far more ambitious path," Dole declared, unveiling his plan in Chicago on Aug. 5, "that puts growth, expanding opportunity, rising incomes, soaring prosperity at the heart of our economic policy."

But a closer look at the Dole plan—and the tortuous way he put it together—reveals much about Dole's thinking and the economic splits rending his party. The plan rewards each key constituency of a fractured GOP: A 15% across-the-board tax cut and the promise of tax reform for supply siders; capital-gains cuts for country club Republicans; a balanced-budget promise for traditionalists; and a \$500-per-child tax credit for social conservatives.

don't come near to paying for the tax cuts (box). Even if all goes according to plan, the package would add \$184 billion to the federal debt during the next six years. And if the additional red ink pushes up interest rates, growth could slow. Even conservatives are skeptical. "It's designed to keep a diffuse coalition together," says William Niskanen, president of the Cato Institute. "It's not really coherent on economic grounds."

SKEPTICS. Many economists and business leaders are even more concerned. "Cutting taxes without a detailed plan [for spending cuts] is not acceptable," says Leonard Miller, chairman of homebuilder Lennar Corp. He's echoed by an executive at a Big Three auto company: "How the heck can you just cut taxes by 15% when the economy is still running substantial deficits?"

The public is skeptical as well: In a BUSINESS WEEK/Harris Poll taken on July 26-31, only 11% of 1,007 respondents said that personal tax cuts were the best way to boost the economy and family incomes (page 38). And unless he follows up with a star turn at the GOP convention, which gets under way in San Diego on Aug. 12, Dole can expect the economic package to give his faltering campaign only a short-lived political boost (page 35).

How was tax hiker Bob Dole persuaded to gamble on a \$548 billion tax cut? The key: convincing the Kansan that he could adopt the theme of rapid growth without fully embracing the sup-

ply-side philosophy he has long horred. Economists Becker and John Taylor, a Stanford University professor who served in George Bush's White House, put the stamp of respectability on growth forecasts by insisting that a broad range of social and economic reforms would contribute as much to shackling the economy as tax cuts. "Dole is genuflecting toward the supply siders," says a top GOP strategist advising the Kansan. "But his measures are consistent with his background."

But getting Dole to adopt even moderate supply sideism wasn't easy. To serve Dole agonizing over this plan is to watch a venerable Republican driven by two desperate imperatives: to narrow the 20-point deficit in the polls and to bridge deep splits in his party. Those drove Dole forward—but his caution held him back, and he repeatedly postponed key decisions. The resulting plan, hammered out during a frenzied weekend of Aug. 2-4, shows the scars of that ordeal.

The path to Dole's growth plan began on May 8, when he and Elizabeth Dole invited economists and fellow senators to a barbecue dinner in his Capitol office. The group agreed that Dole should mount an economic assault on Bill Clinton, tapping into workers' economic anxieties by calling for tax relief and stronger growth. The vehicle offered by Senator Spencer Abraham, a freshman Republican from Michigan: a 15% across-the-board cut in tax rates. Hatched by economic consultant Brian R. Bartlett, a Treasury aide in the Bush

Cover Story

The result of these compromises is an economic agenda that attempts to marry the philosophy of Ronald Reagan with the rhetoric of Labor Secretary Robert B. Reich. Dole vows to ease worker anxiety, narrow income inequality, raise living standards, and hike wages. But his plan could fail for reasons that would be obvious to the old Bob Dole: The proposed spending cuts

ministration, the rate cut was simple harkened back to Ronald Reagan's 6% tax cut in 1981.

The idea found a receptive audience Taylor, who had been advising California Governor Pete Wilson on a 15% in state taxes. Taylor took the lead championing the tax-cut idea among academics. Some economists, notably Harvard University's Robert J. Ro, argued for more fundamental reforms, such as replacing the income tax with a sales tax or a levy that exempts savings. But Dole wasn't ready to go that far.

The other key participant was Senate Budget Committee chairman Pete V. Domenici (R-N.M.). Dole's ally through a decade of budget battles, Domenici is deeply hostile to cuts that might bust the budget. As the plan evolved, Dole would be counting on him to decide whether spending could be squeezed enough to balance the budget while cutting taxes. "Pete's assurance would be very important to Dole," says a campaign official.

MP CHIMES IN. Although Dole wasn't ready to commit publicly to a plan immediately after the confab, Taylor's no summarizing the discussion set a direction: tax cuts first, with a promise of fundamental reform by 2000. The program infuriated former Housing and Urban Development Secretary Jack F. Kemp. The dean of supply-siders had won his weight behind sweeping tax reform, along the lines of the 17% flat tax championed by Forbes. Rate cuts, Kemp feared, would take the steam out of a radical overhaul of the tax code. Kemp summoned his supporters to devise a strategy to derail Dole's plan. To the supply-side faithful, eager to convert Dole, wouldn't join in. So he shifted gears: In mid-May, he enlisted his plan would wipe out the three top tax brackets—31%, 36%, and 39.6%—led by the deficit-cutting packages of 1980 and 1993. Kemp and Forbes figured the resulting two-rate system would carry them toward flat-tax nirvana.

The dueling tax cuts slowed Dole's ready ponderous decision process. Dole's aides pushed for a late-May rollout of a plan as the camps squabbled. On June 1, Dole shook up his team by installing co-policy director an old friend, former Ford White House Chief of Staff Donald H. Rumsfeld, who had since resurrected G.D. Searle & Co. and General Instrument Corp. Rumsfeld was red with a supply-side favorite, former Representative Vin Weber (R-Mn.). Finally, GOP traditionalists and supply-siders were working together, albeit uneasily.

The new team broadened, then nar-

WHERE SPENDING WOULD HAVE TO BE SLASHED

If candidate Bob Dole's \$548 billion tax cut propels him into the White House, President-elect Dole would wake up on Nov. 6 facing an enormous challenge: how to find the huge spending reductions his plan implies.

He wants to cut taxes and still balance the budget by 2002, while sparing three-quarters of federal spending from the ax. By his own reckoning, Dole will have to come up with \$832 billion in savings over six years—enough to finance his tax cuts, plus \$284 billion in additional payments beyond what's already been budgeted to reduce the deficit.

Where on earth does he come up with that kind of dough, with politicians in both parties so fearful of making deep spending cuts? From popular programs, such as Medicare and environmental protection.

But candidate Dole knows it's bad politics to admit that now. Congressional Republicans got their political heads handed to them last year when they tried to pass a budget plan calling for \$650 billion in savings over seven years. Dole's advisers have made his job a little easier by updating the old supply-side nostrum that lower tax rates lead to greater economic growth and revenues. In the 1990s version, education subsidies and deregulation—as well as tax cuts—generate more growth. But even Dole's economists could only find \$147 billion in fiscal free lunch—the so-called supply-side effect. "Dole's package is only halfdone," says David M. Jones, chief economist at Aubrey G. Lanston & Co. "Where are the spending cuts to pay for them?"

To keep bond-market vigilantes off

his back, President Dole would still have to find at least \$685 billion in actual spending cuts. A small chunk would come from Medicare. By embracing last year's GOP budget plan, Dole grabs about \$160 billion in savings, trimming about 10% from anticipated spending. He would get an additional \$70 billion or so from Medicaid. But Social Security is "off the table" according to Dole. So is defense spending. The bulk of the cuts—more than \$400 billion—would have to come from all other domestic programs, from national parks to highways.

GOP lawmakers concede they could never pass such a draconian plan, which would mean a 30% cut after inflation. Yet Dole would slash \$217 billion on top of that—\$136 billion in undefined "administrative" and "other" spending (table). Those cuts are squishy: Dole says he can save \$15 billion a year by hacking administrative costs 10%—the White House says that would only glean about \$2 billion.

Where else can Dole get the money? He could cut corporate subsidies and nick the defense budget. But the real money remains where it always has been: in entitlements such as Medicare and Social Security, which are expected

to account for 60% of all government spending in 2002. If Dole becomes President, look for him to appoint a bipartisan commission to "save" those programs. And don't be surprised if the commission incidentally finds the cash to pay for his generous tax cuts.

By Howard Gleckman
in Washington

ELECTION '96

ON THE TABLE

OVERHEAD Cut administrative

costs by 10% from all federal departments and agencies

\$100 BILLION

CABINET AGENCIES Veterans and Energy and Commerce Dept.

\$17 BILLION

DISCRETIONARY SPENDING Housing

by 12% after spending, which would be \$100 billion in 2002

\$12 BILLION

ASSET SALES Sell part of the

government-owned assets

\$14 BILLION

TOTAL \$217 BILLION



CLOSE UP COMMERCE? Dole needs \$832 billion in savings

rowed, the tax-cut options. Rumsfeld pushed for decisions, only to see Dole move in agonizing half-steps. "We had a guy on the road five days a week who wanted to micromanage every decision from his plane," recalls one campaign source. Dole continued to fret that he would be criticized for busting the budget. By early July, he was back where

he started: torn between two tax packages, with no way to pay for them. The breakthrough came on July 11. Dole dropped in on his advisers, only to stay more than two hours while Becker and Forbes debated how much growth the Dole plan could produce. "That night, Dole was really fixated," says one insider. "He kept saying, 'Look, what kind of numbers can we realistically expect to get?'" Forbes argued that lower tax rates would ignite an explosion of work output and savings. Judy Shelton, an economist from Empower America, Kemp's think tank, insisted that cutting the capital-gains rate would "unlock" \$7 trillion in assets that investors would sell and pay taxes on. The supply siders maintained that 50% of the \$500 billion tax cut could be recouped by 2002.

But Dole was swayed by Becker, who argued the gain would be more like 30%. What mattered most to Dole, though, was assurance from the Chicago economist that growth wouldn't be due to tax cuts alone. Becker explained how regulatory reform, school choice, and worker training—issues Dole had long championed—could also boost the economy by making workers and firms more productive. Becker and Taylor dubbed this the "income growth effect"—a foggy way of saying that higher growth

would produce more tax revenue. Satisfied, Dole locked in a target of 3% long-term growth and left convinced that his plan could achieve it.

By July 20, Dole's conversion was complete. Appearing at a Saturday morning session in khakis and a button-down dress shirt, Dole took command of the meeting. "He knew all the numbers, all the options, the timing," recalls Shelton. Domenici, too, gave his blessing, telling Dole: "This is doable in budgetary terms." The next week, Rumsfeld and Domenici appeared at a Kemp-sponsored press conference to announce Dole's tax-cutting credentials.

Which tax cut, though? Forbes, working inside the campaign, and Kemp, sitting outside, kept up the pressure to eliminate top rates. Taylor fought for the 15% cut, aided by Senators Abraham, Domenici, and Connie Mack of Florida. "The guys who've actually w-

Cover Story

he started: torn between two tax packages, with no way to pay for them.

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IS A CHAINSAW THE WAY TO FIX THE IRS?

If you want to make Chris Mitchell's blood boil, merely mention the Internal Revenue Service. Last summer, the owner of American Specialties Inc., a small San Antonio maker of embroidered sportswear, received an IRS notice warning that she hadn't submitted quarterly payroll taxes for her 16 employees—even though she was certain she had. Facing a 90-day deadline before the IRS slapped a lien on her business, Mitchell went down to the wire with dozens of calls to indifferent IRS agents before the agency realized its error: An IRS clerk had inexplicably changed Mitchell's employer ID code to a previous ID number.

Did Mitchell get an apology? Hardly. Three months later, the IRS made the same mistake—making the San Antonio businesswoman relive the Kafkaesque experience. The IRS "needs a clear revamping," fumes Mitchell. "They run roughshod over everybody. There are no limits to what they can do."

Bob Dole is hoping to tap into such seething anger at the polls this November. As part of his sweeping economic agenda, Dole vowed on Aug. 5 to "eliminate the IRS as we know it" by simplifying the tax code, privatizing many of the agency's functions, and reining in IRS auditors who conduct what he calls "KGB-like" probes of taxpayers. "My administration will free the American people from tax tyranny," Dole vows. IRS critics applaud the approach. The Dole proposal, exudes Peter Sepp,

spokesman for the Washington-based National Taxpayers Union, "could help take some of the teeth out of the pit bull."

But some tax experts question whether Dole's reforms would be too sweeping, if not too impractical, to be enacted.

His proposal to allow the 40 million Americans who file one-page returns to simply have their taxes withheld at work would probably provoke a backlash from employers finding themselves juggling extra paperwork. And experts say Dole's proposal to restrict the IRS from conducting intrusive audits conflicts with his desire to shift the legal burden of proof in IRS audits from the individual to the government. "If the IRS had to prove everything, they'd

have to poke into your personal life in ways you'd resent," says Holt Crouch, a Saratoga (Calif.) tax practitioner.

Perhaps more important, critics of the Clinton Administration and where warn that Dole's proposed cut in the IRS's staff by 1999 would peril the agency's ability to maintain voluntary compliance rate that, at only 83%, ranks among the world's lowest. "These proposals would bloat the budget deficit, penalize the vast majority of taxpayers who pay all of the taxes, and undermine respect for the law," says Deputy Treasury Secretary Lawrence H. Summers.

Other skeptics fear that Dole's plan to provide a one-year amnesty to tax delinquents might turn into a budgetary black hole. While Dole is banking on the

ELECTION '96

THERE COULD BE A STAMPEDE FOR TAX SHELTERS

Bob Dole says the tax cuts in his economic plan will "unleash the full potential of the American people once again." But some tax experts believe the proposal could unleash something else: new shelters for wealthy investors.

Certainly, no one is predicting a return to the classic tax scams of the 1970s and 1980s. Then investors plowed money into almost-certain money losers such as oyster farms and vacant office buildings, claiming generous passive-loss allowances that let them shelter other income. Congress

closed most of those loopholes with tax reform in 1986.

But Dole's plan offers a tantalizing opportunity: He would slash the rate for capital gains in half, to 40%, while lowering the top marginal rate for ordinary income only slightly to 34%. For tax pros, that's going to be an almost irresistible invitation to devise new ways to leverage the strategy. "There would be a greater incentive to camouflage ordinary income with capital gains," predicts John Wilkins, a senior Treasury Dept. tax policy official.

How would the new tax-avoidance

ctions are for the 15%," one Dole e noted sarcastically. But Dole didn't decide until Saturday, Aug. 3—two days before his scheduled speech in Chicago. The clinching argument: The 15% cut was easy to explain and gave all income groups a proportional tax cut. Eliminating top rates would tilt the benefits to the rich, requiring other complex steps—such as reductions for Social Security payroll taxes—to balance out the plan. With the centerpiece set, the economic team scurried through a weekend. To limit the impact on the deficit, the reduction in rates would be phased in—5% in 1997, 10% in 1998, and 15% in 1999. Dole's earlier plans to cut the gasoline tax and offer new small-business tax breaks were junked. To assuage growth concerns, Dole decided to halve the capital gains rate, to 14%, below the 19.8% rate

of new tax revenues generate, skeptics say also send a signal that the deficit doesn't matter. They cite similar state programs providing revenue windfalls but didn't all prove compliance—and some emboldened a whole new group of scofflaws to wait for the next nesty. "Most taxpayers are rightfully annoyed at the next-door neighbor who pays late and nesty," says Joseph A. Menlo Park, a licensed representative before the IRS. Initially, candidate Dole's proposals that the IRS would cause troubles for Dole if he were elected. Because the plan might reduce revenues Dole would need to balance the budget. Indeed, even such fellow bashers as House Ways &

as work? Some analysts pre-empted interest in real estate derivatives. Another possibility: Derivatives by Wall Street wizards that investors take short-term losses at a rate for ordinary income looking profits at the 14% capital gains rate.

SEASON. Of course, there will be a lot of economic benefits from the tax plan. Managers would be encouraged to take more of their stock or options, which are taxed as capital gains—pre-empting giving them greater incen-

passed by the GOP Congress in 1995. Social conservatives such as Christian Coalition leader Ralph Reed and conservative values czar William J. Bennett got their \$500-per-child tax credit, phased in over two years. And to score points against Clinton's 1993 tax increase on upper-income retirees, Dole proposed cutting the share of Social Security benefits subject to tax from 85% to 50%.

The team spent much less time debating how to pay for the tax cuts. Once they

settled on the growth payback—\$147 billion, or 27% of the tax-cut package—the economists adopted several simple ideas to get there: Trim Washington's spending on paperclips, close two Cabinet departments, and auction more airwaves. Dole also pledged to sock it to the tax man, proposing a 30% cut in IRS staffing by 1999—a move that could imperil the agency's ability to round up revenues (box).

The plan is clearly ambitious. But is Dole holding a royal flush? Or will his wager turn out to be little more than a riverboat gamble—former Senate Republican Leader Howard H. Baker's memorable description of Reagan's supply-side experiment? If Dole can boost long-term growth to 3.5% a year—a 50% increase—it will be a monumental achievement.

But most private economists and many business executives say they

mittee's efforts to slash the IRS's fiscal 1997 budget by 8%, to \$6.75 billion. Perhaps mindful of Administration estimates that every dollar in IRS budget cuts costs \$4 in lost tax revenues,

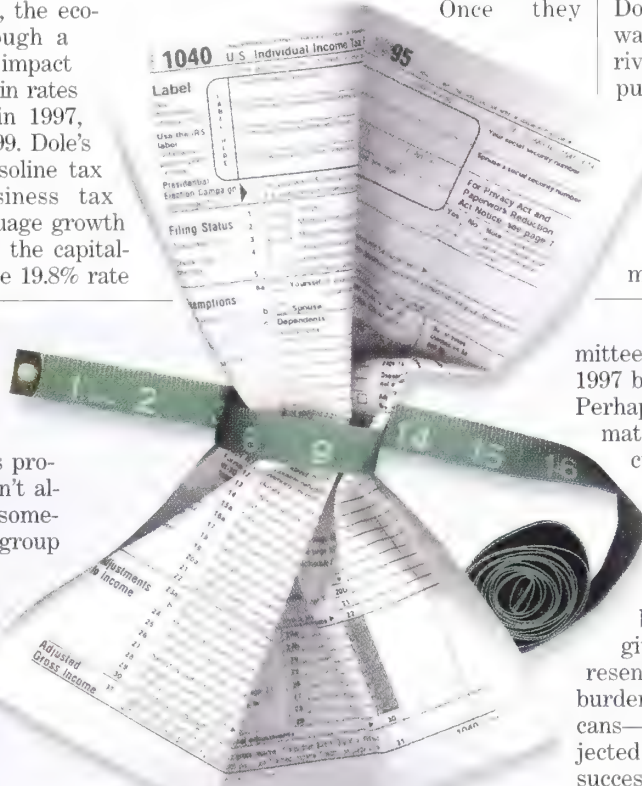
Archer warned that "substantial federal revenues could be lost, thereby exacerbating our federal budget-deficit problems."

To be sure, the IRS has long been a target for public scorn, given its unpopular mission. That resentment has increased as the tax burden has grown for many Americans—and as more taxpayers are subjected to IRS audits. Thanks to the IRS's success in automating more functions, the agency conducted a record 1.9 million audits last year, nearly 50% more than in 1991.

STREAMLINING? At times, though, the agency can be pretty heavy-handed. Particularly irksome to many taxpayers are the controversial "lifestyle audits" that IRS agents have conducted in recent years when they suspect that taxpayers' living standards grossly exceed their reported income. Dole now wants to end such audits, which involve deep probing into the individual's personal spending, except in cases of clear criminal behavior.

Experts believe that Dole, if elected, might better succeed by attempting to streamline a tax code that has become complex and unwieldy. "The only way to create a better IRS is to simplify the tax code," says Stuart Kessler, senior tax partner for New York-based Goldstein Golub Kessler. And that approach might avert a revolt by taxpayers like Chris Mitchell.

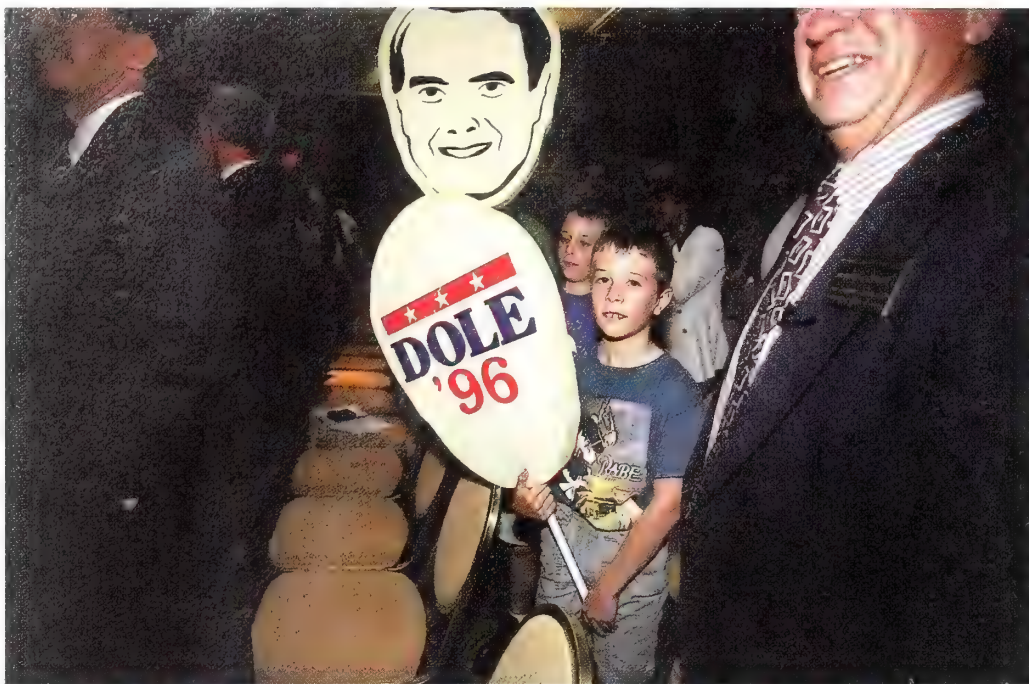
By Dean Foust in Washington



Means Committee Chairman Bill Archer (R-Tex.) have come to realize the limits to their rhetoric: Despite his frequent attacks on the agency, Archer in late June opposed a House subcom-

mittee to perform well. And investors would have more reason to buy growth-company stocks that don't pay dividends.

But the biggest winners of all may be the brassy tax lawyers who lost many of their lucrative shelters over the past decade. And Dole's plan to get rid of thousands of Internal Revenue Service auditors would leave fewer tax cops to crack down on shady schemes. Warns Deputy Treasury Secretary Lawrence H. Summers: "It could be open season for tax shelters." Have your calculators at the ready.



wouldn't bet much on the plan. At best, they say, it would increase the rate of growth by a fraction of a percentage point in coming years. Every tenth of a percentage point increase in growth means an extra \$70 billion for American workers and investors. That's real money, but it won't really change an economy in the midst of a dramatic transition. "It's a proposal that—if paid for—should spur labor supply and investment modestly," says former Congressional Budget Office Director Robert D. Reischauer. "But the fundamental reasons why we have slower growth can't be changed by magical tax plans or spending proposals." One major reason the economy is expanding more slowly than in the 1960s is that the labor force isn't growing as fast. And no President can do much about that.

KICKING BACK? With slower population growth, the key to higher growth without inflation is more productivity. Dole's across-the-board rate cut may provide an incentive for some middle-income people to work harder, since they would keep more of what they would make. But it could as easily induce the wealthy

Dole also would turn federal job-training programs over to the states in a bid to boost job skills and productivity. But neither move will produce the kind of quick growth that Dole is counting on.

Labor is only half the story. The rest is capital. And some of the Dole tax cuts are geared toward encouraging more investment. Cuts in both marginal rates and in the capital-gains rate should, in theory, boost investment, since after-tax returns will rise. "If he can improve investment, he could well achieve growth in the economy without inflation," says Eric Tomlinson, CEO of GeneMedicine Inc.

Much of that incentive, though, is diluted by other Dole proposals. The \$500-per-child tax credit is likely to spur consumption, not investment. So are a new tax credit for charitable donations and the rollback in taxes on retirees. Worse, not all new investment may be productive. The big gap between a 14% capital-gains rate and a 34% top rate on earned income could mean a return to the world of pre-1986 tax shelters (page 32). "As long as interest payments are still deductible, it doesn't make sense to have a preferential capital-gains rate," says Cato's Niskanen.

Can any economic plan deliver the payoff Dole promises? Reagan's 1981 fiscal plan provided a powerful test (page 36). His tax cuts are still being touted by supply siders as kicking off a burst of economic growth. But the evidence shows strongly that much of the 1980s' growth in investment and the labor force

DOLE KIDS

The \$500-per-child tax credit, designed to mollify conservatives and spur savings, would more likely pump up consumption

was due to a strong recovery engineered by the Federal Reserve's tough inflation-fighting policies.

Four years after the 1981 recession hit bottom, economists at WEFA Group Inc. found, labor force growth indeed outpaced normal expansions, but only by a small amount. Capital spending actually lagged behind a typical expansion. WEFA chief economist Daniel Bachman says the Reagan experience shows just how hard it is for tax policy to buy powerful demographic trends and the business cycle: "To get the effect Dole wants, you'd have to have massive changes in labor force participation.

Without such change, Dole's plan isn't likely to boost growth by much. If it blows a hole in the deficit, all bets are off: His growth agenda will end in a Carteresque scrap heap of well-intentioned but failed economic plans. Skyrocketing interest rates set off by panicky bond traders and a none-too-pleased Fed could derail the economy.

Already, analysts doubt whether Dole really has a way to pay for tax breaks. His spending cuts are sketchy, and aides are unwilling to fill in details. A quarter of the tax cuts are financed by Dole's "income growth effect." Another \$225 billion comes from cuts in Medicare and Medicaid included in the year's GOP budget package. Dole says other entitlement cuts are "off the table."

That leaves more than \$400 billion to come from deep but unspecified cuts in other domestic spending. Clintonites ridicule the magnitude of these reductions: "The FAA will be watching out of every three planes," scoffs a senior Administration official. But even allowing for political hyperbole, the cuts would be huge. After inflation, a broad range of federal programs would have 40% for their operations by 2002.

Such dramatic cuts would push most federal programs—including community development, mass transit, highway and environmental protection—back to the states. That policy, which Ohio's Republican Governor George V. Voinovich used to call "shift and shaft," would mean higher state and local taxes.

Dole's decision to exempt defense, Social Security, and most of Medica

Cover Story

to kick back: If after-tax pay is up, why not spend more time on the boat?

Of course, the economy could always make better use of the people it has. Here Dole's ideas have some merit, economists say. He proposes converting \$12 billion in educational aid into vouchers that would promote school choice, figuring competition will force schools to turn out better educated workers.

the cuts has budget hawks furious. The thing that disappoints me most is that once again the political system doesn't seem to lend itself to an intelligent discussion about what to do about entitlements," says David H. Resler, chief economist at Nomura Securities International Inc. Without real spending cuts, Dole becomes Reagan Redux—backing big tax-

cut goodies and not paying for them. "If you pass the tax cuts without credible fiscal restraint at a time when the economy is close to full employment, inflation and interest rates will rise sharply," says Joel Prakken, chairman of consultants Macroeconomic Advisers.

For more than a decade, Dole has been telling a joke about a bus full of supply siders. The good news: The bus

went off a cliff. The bad: There were three empty seats. Now, Dole seems to have climbed aboard and grabbed hold of the wheel. The question is: Will his plan take the nation down the road to prosperity—or over that precipice?

By Mike McNamee, Howard Gleckman, and Lee Walczak in Washington, with Paul Magnusson in Chicago and bureau reports

COMMENTARY

By Richard S. Dunham

BOB IS BACK IN THE BALL GAME, BUT...

Ah, tax cuts, breakfast of champions. In one bold stroke, Bob Dole has ditched his dour Dr. Pain image for the dashing role of a born-again tax-cutter—and altered the dynamics of the Presidential race. For once, the change is in his favor. By pitting his 15% across-the-board tax cut against President Clinton's call for fiscal prudence, Dole has finally hit on an issue he's confident his rival won't try to co-opt. In the process, Dole may finally build some momentum behind his beleaguered candidacy.

Is tax-cut fever enough to get Dole elected? Probably not, given his lack of appeal to key voter blocs. And a *BUSINESS WEEK*/Harris Poll of 1,007 adults conducted July 26-31 found that a tax cut ranks fourth on America's wish list, behind job creation, government downsizing, and cutting the budget deficit. Still, Dole's offer to boost workers' incomes via the tax code will surely help by putting the White House on the defensive—and reminding voters that Clinton reneged on a '92 call for middle-class tax relief. The plan has "given the campaign a kick start," insists California's Republican Attorney General Dan Lungren.

Others beg to differ. "If the Dole people believe this is going to be their silver bullet, they ought to submit to drug testing," says Claremont McKenna College political scientist John J. Pitney Jr. Indeed, Democrats argue that Dole's sudden embrace of tax cuts is a transparently political pirouette that undercuts his vow to

replace Clinton's tactical shiftiness with Midwestern solidity. Dole's tax cut "is the act of a desperate man rearranging the deck chairs on the Titanic," says Democratic consultant Mark Siegel. "It won't work."

Other Dole flip-flops give the Democrats more ammo. Recently, for instance, Dole has reversed himself on abortion and repealing an assault-

his message. With women creating the majority of new small businesses, he could emphasize how his plan is designed to reduce government red tape for them. And he can try to attract mothers by stressing his voucher program, which lets parents send children to private or religious schools.

Perhaps Dole's toughest sell will be convincing people that an economy that grew at a 4.2% clip in the last quarter really needs a stimulative jolt. An ABC News/*Washington Post* poll conducted Aug. 1-4 found that voters, by an 18-point margin, felt they were better off financially than when Clinton took office. No President has been defeated in this century under similar conditions.

Despite the hurdles he still faces, Dole's tax cuts at least helped consolidate his conservative base. Pat Buchanan's campaign manager, Terry Jeffrey,

blessed the economic plan as "a very good step in the right direction." And supply-side hero Steve Forbes now accompanies Dole on the campaign trail, calling the Kansan a convert to his "hope, growth, and opportunity" mantra.

But that may not be enough. Once tax-cut euphoria fades, Dole still has to cross the threshold of Presidential acceptability. That will take major improvements in style and message—something even admirers aren't sure Dole can pull off.

Dunham covers the Dole campaign for BUSINESS WEEK.

ELECTION '96



"How about this? 'Old Bob Dole is a merry old soul.'"

weapon ban. (First he favored repeal, then he retreated.) The latest Dole reversal came on Aug. 5, when he had to accept a humiliating drive by abortion foes to gut his platform "tolerance plank."

TOUGHEST SELL. The continuing abortion flap complicates Dole's attempt to narrow a potentially lethal gender gap. Among other doubters, Ann Stone, who chairs Republicans for Choice, says nearly half of her 150,000 members will vote for Clinton if Dole does not give new assurances of his desire to respect their views.

To have any hope of closing the gender gap, Dole needs to broaden

LESSONS OF THE REAGAN YEARS

Would a Dole walk on the supply side work any better?

Ronald Reagan's political success made him a model for a generation of Republican pols. But his advocacy of tax cuts and supply-side economics has been regarded with more ambivalence by fiscal conservatives. Until now.

With his plans for a \$548 billion tax cut, Bob Dole is following the path that Reagan laid out. The Economic Recovery Tax Act of 1981, which called for a \$750 billion tax cut—more than \$1 trillion in 1996 dollars—was supposed to spur growth and reverse the torpor of the 1970s. Dole hopes his economic plan will do the same.

Are there lessons in the Reagan experience? Looking back, the Gipper's massive tax cuts for business and individuals did make many Americans better off in the short run. Income rose sharply, as did personal consumption. But the gains came at the expense of bigger budget deficits, sluggish business investment, and lower savings. The budget deficit soared to over 6% of gross domestic product. Rather than increasing savings, as the supply-side advocates had hoped, the national savings rate dropped. And business spending on equipment hardly rose, despite a strong recovery (charts).

Overall, the supply-side policies of the early 1980s had the effect of emphasizing the short run over the long run and eroding the foundation of the economy. Dole's billion-dollar tax-cutting package would likely have much the

same impact: an immediate improvement in living standards, followed by long-term deterioration in the economy's overall strength. "An across-the-board tax cut is a way of encouraging consumption," says Alan J. Auerbach, an economist at University of California at Berkeley. "We should be cutting spending without cutting taxes."

Reagan, of course, was laboring under some handicaps that a Dole Presidency would not face. When Reagan proposed his big tax cut, domestic manufacturers were not prepared for foreign competition, and much of the economic stimulus from lower taxes in the early 1980s fueled an enormous surge of imports. The problem was worsened by the combination of Reagan's defense buildup and the tight monetary policy of the Federal Reserve. Together, these drove the dollar up by 50%, making U.S. industry globally uncompetitive.

Today, U.S. companies are in a much stronger position to take advantage of any increase in demand from tax cuts. Moreover, with inflation under 3% and seemingly quiescent, and government shrinking, the Fed probably won't have to hit the monetary brake so hard.

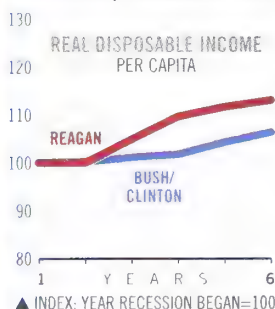
Still, there is little reason to believe that the ultimate effect of Dole's version of supply-side economics will be positive, even if the historical record suggests that Americans might get some very real short-term gains from a tax cut. In 1981, just before the tax cuts passed, federal revenues hit 21% of GDP,

ELECTION '96

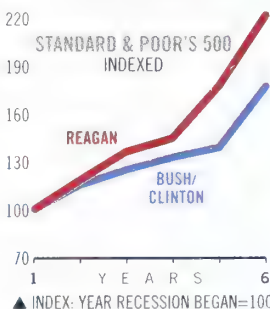
THE HISTORICAL RECORD

It's not always clear the extent of the last recession. In July 1990, for that time, President Bush and Clinton were followed an economic policy of holding down spending and reducing taxes. It's not clear, during the six years that followed the beginning of the recession, whether, as July 1991, President Bush followed a supply-side economic policy of holding down taxes and raising spending. There are the numbers.

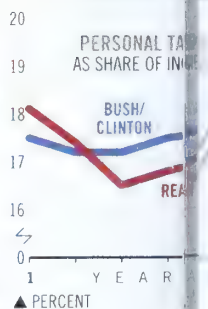
UNDER SUPPLY SIDE POLICIES, INCOMES ROSE...



...THE STOCK MARKET SOARED...



...AND THE TAX BURDEN FELL...





their postwar high. By 1983, that percentage was down below 19%. With a smaller tax bite, disposable income and consumption soared. Tax cuts for businesses and individuals translated into a more buoyant stock market. Adjusting for inflation, the Standard & Poor's 500-stock index rose by 87% from 1981 to 1987, far outpacing the 54% gain of the past six years.

By contrast, over the past six years, revenues taken in by the federal government have risen from 19.5% to 20.5% of GDP. Over the same period, income per capita, adjusted for taxes and inflation, has risen by only 6.5%, half the rate of the Reagan era. Little wonder Americans like the idea of lower taxes.

But the long-term effects of tax cuts on savings and investment—the things that matter for the future health of the economy—are much less positive. A

supply-side tax cut puts more money into the hands of Americans who already spend 95% of every dollar they take in. Certainly, the \$500 credit that Dole proposes to give families for each child will much more likely find its way into new shoes and child care than into a savings account.

MORNING IN AMERICA
Unlike Reagan, Dole wouldn't be bent on an arms buildup—or be faced with a tight-money Fed

Experts on savings behavior agree that cutting the marginal tax rate by 15% is not likely to boost household savings significantly. In the 1950s and 1960s, marginal tax rates were as high as 90%, much higher than today, observes Christopher D. Carroll, an economist at Johns Hopkins University, but Americans saved much more of their income. Says Carroll: "It's hard to believe that there's a strong relationship between marginal tax rates and savings."

In fact, the experience of the 1980s points the other way. Despite the cre-

ation of new savings incentives such as tax-exempt individual retirement accounts (IRAs), the national savings rate fell sharply after the passage of the 1981 tax cuts. The personal savings rate fell from 9% in 1981 to 5% in 1987. Simultaneously, the growing budget deficit ate up a much bigger share of the U.S. savings pool.

Perhaps the biggest danger of a tax

Cover Story

cut is an immediate upward surge in interest rates, even before the cut takes effect. That's what happened in the 1980s, when real rates rose as high as 8% by 1984. With recent memories of double-digit inflation, investors feared that the cuts would lead to big budget deficits—as they did—and reignite inflation. The high rates made borrowing more expensive, and meant that equipment investment stayed at only 6% of GDP, compared with about 8% today.

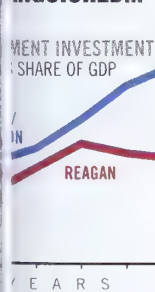
ALL IN THE CUTS. The upward push on interest rates could be eliminated if the budget deficit shrinks. Tax-cutting by itself won't do the trick. Only about 15% to 20% of tax cuts come back in the form of increased revenues, estimates Joel B. Slemrod, a tax economist at the University of Michigan.

That's why the economic soundness of the Dole plan depends more on the ability to achieve its spending cuts, and less on its tax cuts. "If they cut enough spending to balance the budget, then they could get a 0.2 to 0.3% gain in the growth rate," says Joel Prakken, an economist at Macroeconomic Advisers.

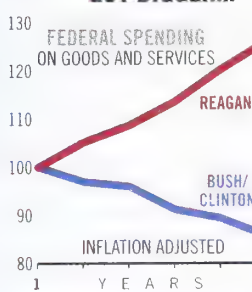
But as Reagan discovered, reducing spending, unlike cutting taxes, requires real sacrifice. From 1981 to 1987, real government spending on goods and services rose by 26%, despite an economic plan which required less spending. That, in the end, may be the most important lesson of the last supply-side experiment.

By Michael Mandel in New York

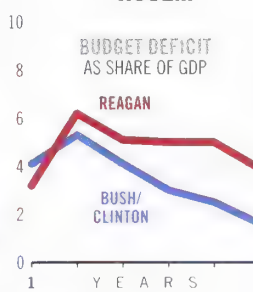
INVESTMENT ANGUISHED...



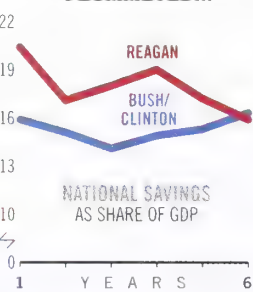
...GOVERNMENT GOT BIGGER...



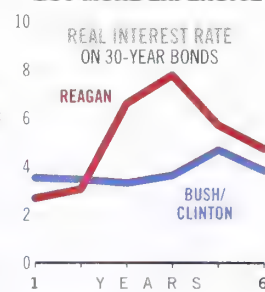
...THE DEFICIT ROSE...



...SAVINGS PLUMMETED...



...AND BORROWING GOT MORE EXPENSIVE



DATA: COMMERCE DEPT., DRI/MCGRAW-HILL, FEDERAL RESERVE, BUSINESS WEEK

LOWER TAXES? SURE. BUT DOUBTS ABOUT HOW TO GET THERE

Tax cuts may be questionable economics—but we'll take them anyway. That's the main conclusion of this poll, taken July 26-31. For most Americans, cutting personal income taxes comes far down on the list of ways to boost the economy. And a stunning 69% of the public says Dole wouldn't be able to both slash taxes and balance the budget. Even so, if a tax



cut of some sort is offered, fully 79% favor Dole's proposed \$500-per-child tax credit, and 65% like the idea of a 15% tax cut.

If the public is happy to take Dole's tax-cut money and run, it's still running straight to Bill Clinton. At the time of the poll, the President continued to lead Dole 45% to 24%, a gap that has held steady in numerous surveys in recent weeks.

Cover Story

IT'S STILL BILL

If the Presidential election were held

today, who would you most likely vote for—Bill Clinton for the Democrats or Bob Dole for the Republicans or a third-party candidate such as Ross Perot or Richard Lamm, or would you not vote at all?

Bill Clinton	45%	Would not vote	16%
Bob Dole	24%	Another candidate.....	2%
Ross Perot/		Don't know	2%
Richard Lamm	11%		

NOT MUCH HELP FOR THE ECONOMY

Bob Dole says America needs a large personal income-tax cut now to boost the economy and raise family incomes. Do you think such a personal income-tax cut will help the economy a lot, help the economy a little, hurt the economy a little, hurt the economy a lot, or not make any difference?

Help a lot	15%	Hurt a lot.....	8%
Help a little	27%	Not make any difference ..	34%
Hurt a little.....	10%	Don't know	6%

JOBS ARE ANSWER 1

I'm going to read you a list of things that might be used to help the economy and raise family incomes. Which of these do you think will be most effective in helping the economy and raising family incomes?

Creating jobs.....	40%	Cutting personal	
Downsizing government	26%	income taxes.....	11%
Reducing the federal		Assuring fair trade	5%
budget deficit	15%	Don't know	3%

LOVE THAT KID CREDIT

Here are some ideas that Bob Dole is considering as part of his economic plan. Do you favor or oppose that idea?

	STRONGLY FAVOR	SOMEWHAT FAVOR	SOMEWHAT OPPOSE	STRONGLY OPPOSE	DON'T KNOW
Giving an additional \$500 per child credit to families	49%	26%	9%	11%	5%
Cutting the federal income tax rate by as much as 15%	37%	28%	14%	15%	6%
Allowing individuals to deduct from their income tax a portion of the payroll tax they pay for Social Security*	27%	28%	18%	18%	9%
Cutting the rate on capital gains from the sale of houses, stocks, and other investments	29%	25%	18%	17%	11%
Lowering the top tax rate for high-income taxpayers to 28% from 40%*	22%	18%	17%	37%	6%

YES, TAXES NEED FIXING

Bob Dole says that his long-term goal is to overhaul the tax code to move to a simpler system with lower rates but fewer deductions. Do you strongly agree, somewhat agree, somewhat disagree, or strongly disagree with this goal?

Strongly agree	28%	Strongly disagree	13%
Somewhat agree.....	39%	Don't know	3%
Somewhat disagree.....	17%		

SKEPTICAL ABOUT PAYING THE PIPER

Here are some of the ways that Dole says he will pay for his tax cuts. If Dole is elected President, how likely is it that he will be able to do each of the following in order to lower taxes—very likely, somewhat likely, somewhat unlikely, or very unlikely?

	VERY LIKELY	SOMEWHAT LIKELY	SOMEWHAT UNLIKELY	VERY UNLIKELY	DON'T KNOW
Eliminating some government agencies.....	19%	31%	21%	25%	4%
Relying on tax cuts to produce higher growth and so, more revenues for the Treasury	8%	30%	28%	27%	7%
Reducing tax breaks and subsidies for corporations	9%	28%	27%	32%	4%
Slowing spending on social programs such as Medicare and Medicaid	10%	23%	27%	36%	4%
Selling off government assets such as the airways used by broadcasters	10%	23%	26%	31%	10%

MORE MIDDLE-CLASS PAIN? PROBABLY

President Clinton says the only way Dole can pay for tax cuts of this size is through large cuts in programs for the middle class and the poor such as Medicare, Medicaid, welfare, and education. Do you strongly agree, somewhat agree, somewhat disagree, or strongly disagree with President Clinton?

Strongly agree	34%	Strongly disagree	21%
Somewhat agree	27%	Don't know	2%
Somewhat disagree	16%		

IMPOSSIBLE BALANCING ACT

Dole has said he plans to cut taxes by up to \$600 billion over the next six years and still balance the budget. Do you think it is possible to both cut taxes and balance the budget, or not?

Possible	28%	Not possible	69%	Don't know	3%
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EDITED BY KEITH H. HAMMONDS

Survey of 1,007 adults conducted July 26-31, 1996, for BUSINESS WEEK by Louis Harris & Associates Inc. Results should be accurate to within 3 percentage points.

*These items ultimately were not included in Dole's economic plan.

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THE STATES

WELFARE TIME BOMB?

Federal reform has states edgy about hiked costs and lost innovation

For two years, Minnesota has been at the forefront of welfare reform, experimenting with a pilot program that has shifted 36% of aid recipients in eight counties into work. But now, officials are rushing back to the drawing board. A new federal law will require every state to place half its welfare population in jobs by 2002—a timetable few officials feel they can meet without huge sacrifices. "This will become more difficult than putting a square peg in a round hole," worries John Petraborg, Minnesota's Acting Commissioner of Human Services.

By mid-August, President Clinton is expected to sign legislation enabling the most radical welfare reform since the system was crafted 60 years ago. When he does, governors will get what they long clamored for—control over entitlement programs serving 12.8 million poor and 1 million legal immigrants. They may soon wish they had kept quiet: The bill will require a wholesale restructuring, even as projected funding is reduced over six years by \$56 billion.

The legislation could also mark the start of the long-feared "race to the bottom," a competition to cut benefits in the name of fiscal prudence and economic competitiveness. "It will be tempting for some governors to focus on more popular areas for spending," such as economic development, says Cynthia Eisenhauer, director of the Iowa Workforce Development Dept. Officials also worry that generous benefits will lure legions of the poor from other states. Minnesota Governor Arne H. Carlson

says he may even impose a law to limit new arrivals to the benefits they received where they had been living.

Minnesota is better off than many states. Consider Florida, where welfare reform is expected to leave a \$550 million hole in funding for the state's growing legal immigrant population. The new legislation will cut off federal aid for food stamps, Medicaid, and supplemental Social Security to immigrants. And Florida cannot make up the difference from its own coffers without major policy changes or tax hikes. "This is a huge problem," seethes a spokeswoman for Governor Lawton Chiles. "We have pockets of elderly immigrants who will be drastically affected."

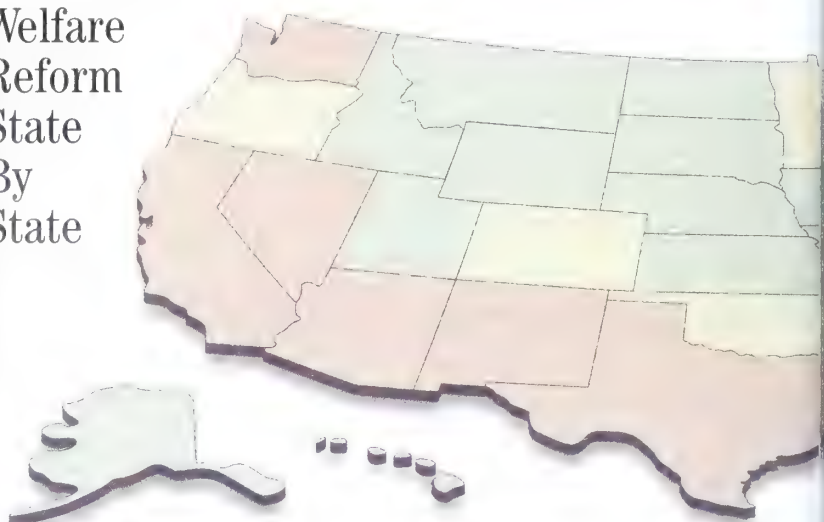
"GOING TO BE STRAPPED." The sense of alarm is mounting. "We're all going to be strapped for more capital," frets Colorado Governor Roy Romer. Two chief areas of concern: how to pay for immi-

grant benefits and how to take more people off the dole, particularly among the first easy-to-place people find jobs. Tremors are rippling through New York City, which could be required overnight to quadruple participation in its 18-month-old workfare program. Additional child-care bills alone could cost a city up to \$300 million, says Richard Schwartz, senior adviser to Mayor Rudolph W. Giuliani.

Some 43 states already are experimenting with new welfare systems. They will be allowed to continue, but they won't be able to avoid mandates to shift 25% of welfare recipients into jobs within 18 months and 50% by the end of 2002. New enrollees must find work within two years. Certainly, many states will discover room to duck some requirements. "Disaster scenarios are likely to come true in the next year or so," says Paul Peterson, a Harvard government professor. But all states will eventually take a revenue hit. Federal matching grants, which ran as high as 80% of a state's spending and varied with welfare rolls, will be converted into fixed block grants. If states want to pay more for welfare recipients' child care or transportation, they'll have to do so without matching federal funds.

The result: "There's more incentive to simply cut people off," says Timothy Bartik, senior economist at the W.P. Upjohn Institute for Employment Research. Moreover, grants will be tied to the higher federal spending of several years ago, but the cushion is "small."

Welfare Reform State By State



? Questionable Impact

States that likely will see their welfare rise as a result of federal reform, because they are home to a relatively high percentage of legal immigrants, have a low percentage of employed welfare recipients, or post a relatively high unemployment rate.

DATA: CENTER FOR THE STUDY OF THE STATES

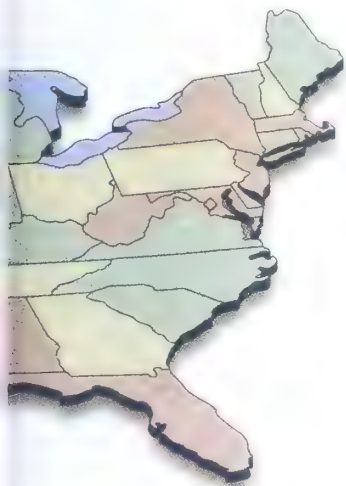
atoes in the face of any recession," says Donald Boyd, director of the Center for the Study of the States.

When the cushion gives out, the impact will fall unevenly across the country. The worst hit, reckons Boyd, will be states with relatively high unemployment, few welfare recipients currently working, and large immigrant populations—states such as California, Florida, Texas, and New York. Larger welfare burdens could have significant impact on the creditworthiness of such states, says Vladimir Y. Dnyk, executive managing director at Standard & Poor's Ratings Group.

Even in states that have made progress with reform, uncertainty runs high. Iowa has shifted 35% of its welfare recipients into work within the past two years—easily the highest level in the nation. Now, though, its education funds are strapped, and federal job-training funds for welfare recipients and the working poor will be cut 23% over the next year. The new federal law may force Iowa to shift all its job-training money into welfare, hurting other workers who need training.

A similarly tricky balancing act faces Minnesota's Petraborg. As it tries to wean the hard-core unemployed into work, the state may have to cut spending on social services for those already in low-paying jobs. "The pressures are increasing significantly," he says. Few would dispute that the old welfare system was broken. But state officials are already wondering whether a leap into the unknown will improve their lot.

By Richard A. Melcher in Chicago, Keith H. Hammonds in New York and Gail DeGeorge in Miami



ates less at risk, because they are home to a lower percentage of legal immigrants, are welfare recipients who are working, or have a lower unemployment rate

COMMENTARY

By John Pearson

GIVE ME YOUR HIGHLY SKILLED, YEARNING TO SUCCEED

Some 785,000 resident aliens collected U.S. Supplemental Security Income (SSI) payments last year, and around 550,000 drew checks under Aid to Families with Dependent Children. The cost to American taxpayers, not counting noncash aid such as food stamps: more than \$5 billion.

The problem is growing. In 1997, legal immigration will surge to 854,000, while illegal immigration keeps adding an estimated 300,000 people per year. Meanwhile, polls show that a large majority of Americans, including most naturalized immigrants, favor reducing both legal and illegal immigration.

President Clinton has promised to sign a welfare reform bill that would deny many benefits to resident aliens. But he will try later, he says, to modify these provisions. He would do better, if reelected, to lead an effort to address the underlying problem: a flawed immigration system. We currently give preference to immigrants' family members—so-called chain migration—regardless of their skills and education. We ought to allocate more spots to highly trained workers who can make the U.S. economy more competitive.

NO SIBLINGS. A solid starting point should be the blueprint laid out by the U.S. Commission on Immigration Reform, headed by former Representative Barbara Jordan (D-Tex.) until her death last year. Its proposals call for reducing immigration to an annual 550,000—including 400,000 through family reunification, 100,000 skilled immigrants, and 50,000 refugees. To reunify nuclear families, immigrants would be allowed to bring in spouses, minor children, and parents, but chain migration would be ended by eliminating preferences for other relatives, such as brothers and sisters. That would remedy a big flaw in the current system, in place since 1965, under which 460,000 immigrants' family members represented 64% of all entrants in 1995—and under which the



LOST FRONTIER: By 2050, there may be 400 million Americans, vs. 76 million in 1900

number of entrants grows every year.

Earlier, even more open immigration policies doubtless allowed the forebears of many BUSINESS WEEK readers to come to the U.S. But while U.S. industry today desperately needs skilled workers, our current system draws in immigrants with ever lower skill levels, according to studies by Harvard University economist George J. Borjas.

This year, business lobbying on Capitol Hill helped derail any change in legal immigration rules after high-tech companies became alarmed at a proposal to reduce to 90,000 the 140,000 cap on employment-based immigrants. Businesses last year sponsored only 10,500 highly trained professionals, but spokesmen say they are worried about moves to limit personnel transfers. The business lobbying has turned congressional sentiment against any legal-immigration reform, Capitol Hill observers say.

That's a mistake. Under the current system, not only are we bringing in immigrants less likely to contribute to society, we are expanding the population at a rate that strains the environment. By 2050, there will be nearly 400 million Americans, the Census Bureau projects, if immigration continues at about 1 million annually; that compares with 76 million in 1900. Today's America requires a new immigration policy. Given our needs in the global economy, we must be more selective about whom we allow in.

Pearson covers Latin America and international business.



PEOPLE

ROCKWELL'S TRICKIEST LAUNCH YET

CEO Beall hopes Wall Street will laud its top-down makeover

Donald R. Beall is a deliberative man. Through a decade of upheaval in the defense business caused by government spending cuts, Rockwell International Corp.'s chief held tight, neither selling nor adding much to his company's defense and aerospace businesses. Finally, last fall, Beall began shopping the units around. On Aug. 1, he made his big move, selling what long had been the heart and soul of the company to Boeing Co. in a stock and debt deal worth \$3.2 billion.

The transaction may mark the start of a lot more action at Rockwell as Beall tries to remake it into an electronics powerhouse. Key to the strategy: a big acquisition or two. The Boeing deal leaves Rockwell cash rich, with some \$4 billion in what Beall calls financial "firepower" that could be used for such deals.

Along the way, the CEO hopes Wall Street will take a new look at Rockwell. In the fiscal year ending Sept. 30, Rockwell says operating earnings of the slimmed-down company will hit \$1.2 billion on revenues of \$10.4 billion. "Our performance has been terrific," says Beall. "This company should be revalued." His goal: to garner a price-earnings multiple comparable to the ones paid for admired companies such as AlliedSignal, General Electric, and

Hewlett-Packard (chart). "Don has a very clear vision of where he is taking Rockwell," says Boeing CEO Philip M. Condit. "When you take a company in a fundamentally new direction, that's not an easy thing."

Indeed, the question now is whether Beall, with his steady nature and conglomerate background, can remake Rockwell into a growth company. Beall, 57, is a hard driver from humble beginnings. As a youth, he made money by pumping gas along the commercial-fishing wharf in Crescent City, Calif., in the afternoons and loading lumber barges in the evening. He first joined Rockwell at 28 and has spent most of his career there. He was named president and elected to the board at 39 and has been CEO for 10 years. Wall Street credits him with building up key businesses such as industrial automation. But he also has been criticized for failing to restructure the company fast enough. To this day, some analysts

U-TURN

Beall aims to make Rockwell a powerhouse to rival General Electric and H-P

gripe that he might have gotten a better price for the defense units he had sold earlier.

Now that he's moving, Beall's main focus will be continuing to expand Rockwell's \$4 billion industrial-automation business. The company became the biggest player in the U.S. market after its acquisition of Reliance Electric Co. last year for \$1.6 billion. Since then, it has been snatching up market share in industries ranging from autos to pharmaceuticals. Beall hints that the next large deal is likely to be in Asia or in Europe,

where in 1993 he acquired Speeder+Schuh, a Swiss maker of automation gear, for \$105 million.

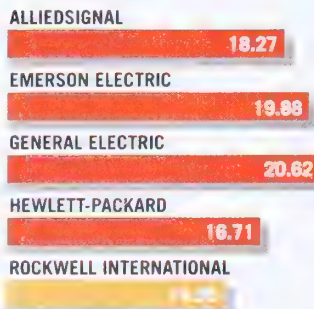
GOOD PROSPECTS. Rockwell's other big business is its fast-growing \$1 billion semiconductor unit. For the past several years, the chip business has surged. It supplies 80% of the chips that go into fax machines and 65% of those that go into modems for personal computers. And it has good prospects for growth: Rockwell also makes the guts for digital cordless phones, potentially a big consumer-electronics product. On July 1, it moved into the exploding multimedia graphics market when it acquired Brooktree Corp. for \$275 million. Despite a slowdown in other areas of the chip market, Beall says Rockwell's sales will nearly double this year. Still, he's delaying for about a year construction of a new Colorado Springs (Colo.) plant in which Rockwell is investing \$1.2 billion.

Meanwhile, analysts and some investors want Beall to do more restructuring. He already shed the company's printing press business in April. Now, pressure is mounting to sell off Rockwell's poorly performing automotive unit, which has been marred by warranty problems and strategic missteps such as its ill-timed recent expansion in Brazil. Messing around, remaking a conglomerate.

By Eric Schine
Seal Beach, Calif.

BEALL'S BIG CHALLENGE

ROCKWELL'S PRICE-EARNINGS MULTIPLE VS. PEERS**



*BASED ON TRAILING 12 MONTHS' EARNINGS PER SHARE
DATA: BLOOMBERG FINANCIAL MARKETS

THE WOMAN AT CENTER COURT

won't be a layup for Val Ackerman, new WNBA prez

As a small forward on the women's basketball team at the University of Virginia in the 1970s, Valerie Ackerman racked up some 1,500 career points. But the 5-foot, 9½-inch player developed a reputation for physical play. Her style, Ackerman concedes, generated a lot of heated discussion with the referees.

These days, Ackerman is again involved in heated discussions about basketball—but this time, she's in a business suit. On Aug. 7, Ackerman, 36, was named president of the Women's National Basketball Assn., which will launch next summer as an offshoot of the NBA.

Ackerman has her work cut out for her. To make the WNBA succeed, she

needs to sign as many top players as possible before the rival American Basketball League lures them away. ABL co-founder Gary Cavalli says he has already signed nine U.S. Olympic team players. But several top names, including Sheryl Swoopes, plan to sign on with the WNBA.

Other attempts to launch female basketball leagues have failed—one as recently as 1991. But the WNBA has some key advantages. To begin with, the NBA is betting heavily on its sister league. When eight WNBA teams start up, NBA teams will be responsible for administration of the women's clubs.

THREE CHANNELS. Then there are the television deals. The WNBA's games will be aired three nights a week on national TV—one each on NBC, Lifetime, and ESPN—giving its players maximum exposure and endorsement potential. The ABL, in contrast, just has a deal with SportsChannel America.

The mere idea of regularly televised women's hoops marks a dramatic change from when Ackerman played. At the



IF AT FIRST...

Ackerman faces the sober fact that female leagues have failed as recently as 1991

University of Virginia, she shared the first women's basketball scholarship that the school had ever awarded.

As part of a European team after graduation, Ackerman began thinking that the U.S. needed a women's basketball league. She picked up a law degree at the University of California at Los Angeles and, following a stint at New York's Simpson, Thatcher & Bartlett, was hired by the NBA as a staff attorney.

Will fans used to slam-dunk men's games really stay interested in the WNBA? Ackerman thinks so. The Olympic Games, she says, "showcased our passing, shooting, and intensity." Turn on the TV next summer, she promises, and you may even see women slamming, too.

By Michael Goldstein in New York

COMMENTARY

By Peter Coy

A BUNCH OF DIM BULBS AT THE OLYMPICS

Judging from television broadcasts of the Olympic Games, America has a major problem with flashing. And I don't mean exposing private parts in public places. I'm talking about the ridiculous overuse of flashes by amateur photographers in all sorts of situations where they are of absolutely no use. In Atlanta, every time Michael Johnson or Noureddine Morceli or Gail Devers hit the track, Olympic Stadium turned into the Twinkle Dome.

What's wrong with us, anyway? Don't people know that photo flash can't illuminate anything more than a few feet away? In the stadium, the one thing all those flashes could do was bad—namely, light up stray objects in the foreground of the frame. Automated film developers sometimes expose the frame so the foreground—and not necessarily the subject—comes out properly. That means that more than a few spectators came home with beautiful shots of the straw

hat on that nice lady from Australia a couple of rows down. Beyond the hat: inky blackness.

It's not as if flashes are beyond human control. On most point-and-shoot cameras, the flash can be turned off. As for those cardboard, single-use cameras, it actually takes an extra step to turn the flash on. Nonetheless, photographers continue to use their flash to take shots of, say, Times Square or the Statue of Liberty from the shores of Manhattan. Eastman Kodak Co.'s strategic initiatives director, Terry Faulkner, says

he has seen people using flash bulbs to photograph the light show at Niagara Falls and even a lunar eclipse.

Folks, your flash won't light up the moon—and the eclipse would be spoiled if it could. "There really are people who simply have a flawed understanding, and they believe that the flash is going to work," says Faulkner. But "the main problem is people not knowing how to turn off the flash, or not bothering." In other words, we flash for the same reason we can't set the clocks on our VCRs.

PRIME-TIME FLOP. Ironically, the one time organizers in Atlanta wanted a fury of flashing, photographers failed to cooperate. For the closing ceremonies of the Olympics, volunteers handed out Kodak single-use cameras to all 90,000 spectators, along with instructions on when to trigger their flashes to make a wave of sparkles circle the stadium. The instructions were repeated over loudspeakers during commercial breaks. But when the time came, the globally televised spectacle fizzled to a few isolated pops. Observers theorize that lots of willing participants couldn't figure out how to use the flashes. Figure that.

Coy is a BUSINESS WEEK technology editor.



FUTILE: Atop the Empire State Building

In Business This Week

EDITED BY KELLEY HOLLAND

AOL GOES AWOL

MAYBE THEY SHOULD CALL IT America Offline. On Aug. 7, America Online suffered a massive, nationwide outage of its system after installation of some new software hit a snag. Beginning around 4 a.m., AOL's 6 million customers were unable to sign on to the service. The company said only that the system failure came during some regularly scheduled software maintenance. AOL had a similar problem in February, 1994. While an AOL spokesperson said the company was hoping to have

service restored by the end of the day, as of 6:30 p.m. the system was still down.

FAIR TRADE FOR A COMMODITIES POST?

THREE IS THE MAGIC NUMBER. Early in President Clinton's term, attorney Brooksley Born, 55, was a leading candidate for two key government posts. She didn't get them—but on Aug. 2, the Senate approved her to lead the Commodity Futures Trading Commission. It makes sense: Born has specialized in commodities law at Washington's Arnold & Porter. But her approval did not come without hardball politics. To get full Senate support, Born had to agree to recuse herself from any probe of trading by Hillary Rodham Clinton, a longtime pal.

WHY PFIZER MAY BE IN A BAD MOOD

THE FOOD & DRUG ADMINISTRATION has ordered Pfizer to rein in claims for Zoloft, its \$1 billion rival to Prozac. Contrary to what Pfizer has suggested, the drug is approved only to combat major depression, not anxiety, postpartum depression, obsessive-compulsive disorder, or "mood disorders" such as PMS-related depression. The drugmaker must now run corrective advertising and write to health-care professionals correcting its statements, and the FDA may demand further remedies. Pfizer wouldn't comment.

NETSCAPE GETS TOUGH

THE BATTLE OF THE INTERNET titans just exploded into a legal dispute. In an Aug. 6 letter to Microsoft and the Justice Dept., Netscape Communications' outside

HEADLINER: GARY WENDT

GE CAPITAL'S BIG SPENDER

Gary Wendt isn't the type to take no for an answer. Since 1994, when he was rebuffed by Kemper, the chief executive of GE Capital Services has been buying up insurers at home and abroad.

His latest grab: On Aug. 5, Wendt agreed to pay roughly \$1.8 billion to acquire First Colony, a Lynchburg (Va.)-based life insurer with assets of \$11 billion. That means GE Capital has spent over \$5 billion in the past three years on U.S. life insurers and reinsurers. Included in the shopping spree: Life Insurance Co. of Virginia, Amer-

ican Express' life insurance company, and Great Northern Annuity, formerly a part of Weyerhaeuser.

Wendt has also spent \$1 billion on two German reinsurers.

Wendt has his wallet out because he wants to bring GE's fabled operating efficiencies to bear on these companies. He believes retirement assets will be good business as baby boomers age.

Is Wendt still on the prowl? He said in July that GE Capital's insurance businesses "had not yet reached critical mass." Stay tuned for his next deal.

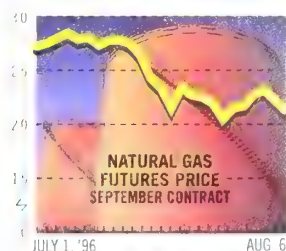
By Tim Smar



CLOSING BELL

FLAMEOUT

The natural-gas rally has gone down in flames. Since July 1, futures prices have plunged from \$2.716 per million BTUs to \$2.124 as of Aug. 6. Cool summer weather in the Eastern U.S. reduced demand for electricity, allowing suppliers to rebuild stockpiles faster than expected. The blow-off turned into a rout as bullish speculators got burned. "It was a wholesale, widespread, and somewhat panicked run for the exits," says Smith Barney analyst John Saucer. As the hurricane season nears, threatening Gulf production sites, watch for more volatile trading ahead.



DATA: BLOOMBERG FINANCIAL MARKETS

lawyer, Gary Reback, accused the software giant of violating antitrust laws. His charge: Newly announced licensing restrictions on Microsoft's Windows NT Workstation software unfairly limit use of Netscape's Web-site software. But that's not all. Reback, whose earlier efforts to curb Microsoft led to a Justice Dept. probe, says he soon may raise objections to Microsoft's deals with AOL and AT&T. Microsoft promised them prominent positions on its Internet connection site if they recommend that customers use Microsoft's Web browser. Justice wouldn't comment. Microsoft called Netscape's move a public-relations ploy.

B&L SEES THE ERROR OF ITS WAYS

BAUSCH & LOMB HAS AGREED to pay as much as \$68 million to settle a class action charge-

ing that it sold identical contact lenses under different brand names at widely varying prices—a tactic first revealed in BUSINESS WEEK on July 12, 1993. B&L denied wrongdoing but says it settled to avoid prolonged litigation. U.S. residents who bought a variety of lenses during a 5½-year period could get cash and coupons on B&L products. The potential payout is well above what B&L earned on the lenses during that period.

ET CETERA...

- Fluor and Westinghouse will get \$11 billion from DOE for clean nuclear weapons plant.
- Pacificare is buying FHP for \$2.1 billion, taking the lead in Medicare managed care.
- Moore abandoned its ye-long takeover battle for Wallace Computer Services.
- Phew. Guess Inc. priced its shrunken IPO, issuing 7 million shares.



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THE SUHARTO EMPIRE

Can the family's big-business deals survive after the President is gone?

For Bambang Trihatmodjo, it was another triumph. Jaws clenched and eyes locked in a fierce gaze, the 43-year-old son of President Suharto was a picture of power, bathed in camera flashes in the Jakarta Convention Center ballroom. On stage, an emcee introduced government ministers and Hyundai Motors Co. executives, who heaped praise on each other. The occasion was the launch of a \$1 billion passenger-car venture between Hyundai and Bambang's Bimantara Group.

As he watched the proceedings, Terry J. Emrick was sullen. A few months before, as Ford Motor Co.'s executive vice-president for Indonesia, Emrick had expected to be launching a new car himself that evening. But instead, Suharto was, again, letting one of his sons launch a sweetheart deal that stacked the deck against other foreign carmakers. So Ford has halted plans to build Escorts in Indonesia. Says Emrick: "We never believed this could happen."

It's yet another case of special privilege. The six Suharto children, along with a few sons-in-law, grandsons, and

other relatives, have come to dominate industry in one of the world's biggest and fastest-growing markets. In the Indonesian version of Camelot, it is well-nigh impossible to get a deal done without a Suharto clan member as ally, agent, or partner. Refusing to cut the Suharto clan into the action means U.S., Japanese, European, and other companies lose out on opportunities in telecommunications, power plants, finance, and automobiles. Says one foreign executive with a big investment in Indonesia: "Without them, you wouldn't have a project. It's as simple as that."

LOOSER GRIP. The fat years, however, may be drawing to a close. Suharto, 75, is said to be in ill health since the death in April of his wife and confidante, Tien. But even if Suharto endures, recent political upheavals in support of opposition leader Megawati Sukarnoputri have sent him a message: Indonesia's political transition may not be smooth.

Suharto, who has ruled with an iron fist since 1966, has yet to designate a successor, and no one child has the clout to inherit his political mantle. "[The transition] could be a disaster because the government is totally centered around one man," says Hilman Adil, director of the Center for Social & Cultural Studies, a government think tank. "Nobody knows what they're going to do after Suharto is not here anymore."

That spells risk not only for his children but also for the foreign companies that have insinuated themselves into



the Suharto business empire. Over the past five years, companies such as Lucent Technologies, Hughes, NEC, Sumitomo, British Petroleum, Deutsche Telekom, and Siemens have forged joint ventures with sons Bambang and Humo Mandala Putra (known as "Tommy") and daughter Siti Hardiyanti Rukmana ("Tutut") (table). The empire, estimated conservatively at \$4 billion, fears that the fortune amassed by former Philippine President Ferdinand Marcos. The Suharto children declined requests for interviews.

One of the most important guessing games in Asia these days is: Which children and their partners are best positioned for the post-Suharto era? Most analysts predict that any successor will be wary of disrupting Indonesia's economy. Should a future President seek to dismantle the Suharto empire, an all-out witch-hunt would be too destabilizing. Practically every big businessman

The Five Suharto Children with the Largest Holdings

	"TUTUT" SITI HARDIYANTI RUKMANA (Daughter, 48)	"SIGIT" SIGIT HARJOYUDANTO (Son, 45)
ESTIMATED ASSETS ('94*)	\$454.5 million	\$454.5 million
EQUITY-HOLDING FOREIGN PARTNERS	Morgan Stanley (planned) Lucent Technologies Marubeni General Dynamics (agent) Motorola (agent)	Mitsubishi Gas Chemical DuPont Mitsui British Petroleum

*At 1994 exchange rates



FIRST-FAMILY ALBUM

Grouped around Suharto and his late wife are, with their spouses, the six children: Sigit (top left), Tommy (top, third from left), Mamiiek (top center), Bambang (top right), Titiek (bottom, second from left), and Tutut (bottom, second from right)

itary leader, or political has benefited.

But there could be some problems, particularly if outside is turned against the Suharto family. Controversial petrochemical deals and the auto projects involving Suharto's sons are the most likely First-Family ventures to be dismantled. Suharto offspring who can't find the right allies in the military could also be exposed. Megawati and her supporters have threatened to break up monopolies and take away the family's privileges.

The big question is whether multinationals will get swept up in retribution. Even if the children are forced to surrender a portion of their assets, most analysts think foreign companies' interests might not be touched. For one

thing, there is a feeling that multinationals had no alternative to collaborating with the Suhartos. And unless there are disclosures of outright bribery or fraud, overturning joint-venture contracts would be difficult because they are legally binding. "The next government may want to redistribute family equity to other investors, but it still must follow international rules," says Jakarta consultant Christianto Wibisono.

Thus, for the Suharto offspring and other relatives, a painful transition seems to be looming. Even if Suharto stays healthy enough to set up a successor who will protect the family's business interests, his family is likely to lose perks such as ready access to investment licenses, cheap credit from

government banks, the ability to acquire the assets of state-owned enterprises at below-market prices, and first dibs on franchises to operate everything from telecoms to toll roads—all without competitive bidding.

Members of Indonesia's First Family are already scrambling to withstand a transition. To improve their chances, they are turning management over to professionals and tapping capital markets. Last year, Bambang listed his 27-unit Bimantara Citra, a holding company with interests in cars, telecoms, infrastructure, and broadcasting, on the Jakarta Stock Exchange. So did Citra Marga Nusaphala Persada, the \$65 million operator of toll roads controlled by Tutut. Says Dorodjatun Kuntjoro-Jakti, economics dean at the University of Indonesia: "The First Family businesses are being forced into the open."

STRANGLEHOLD. For more than a decade, Indonesian technocrats and the World Bank have complained that the family's monopolies and subsidies have driven up commodity prices. In the '70s and '80s, Suharto's sons Sigit Harjojudanto, 45, Bambang, Tommy, and other relatives made their first millions by teaming up with powerful ethnic-Chinese tycoons to become sole distributors of steel, plastics, petrochemicals, and foodstuffs sold in Indonesia.

Then they started using their pull to secure investment licenses and infrastructure franchises. They also piled up wealth by acting as agents for General Dynamics fighter jets, Motorola communications systems, Rolls-Royce engines, and Hughes satellites. Because Suharto approves each investment personally, and since many officials—from ministers to heads of state companies—have lost their jobs by refusing a family request, ramming projects through the bureaucracy has been easy.

They parlayed their relationships into equity stakes in big joint ventures, in most cases without using their own money. In a typical family project, the capital comes from foreign partners and state banks. The children's share, usually 20% of equity, is counted as "goodwill"—

AMBANG

BAMBANG TRIHATMODJO (Son, 43)

18 billion

ghes
utsche Telekom
mens
att
undai

"TITIEK"

SITI HEDIJATI HARIYADI (Daughter, 37)

\$109 million

Edison Mission Energy
General Electric
Merrill Lynch

"TOMMY"

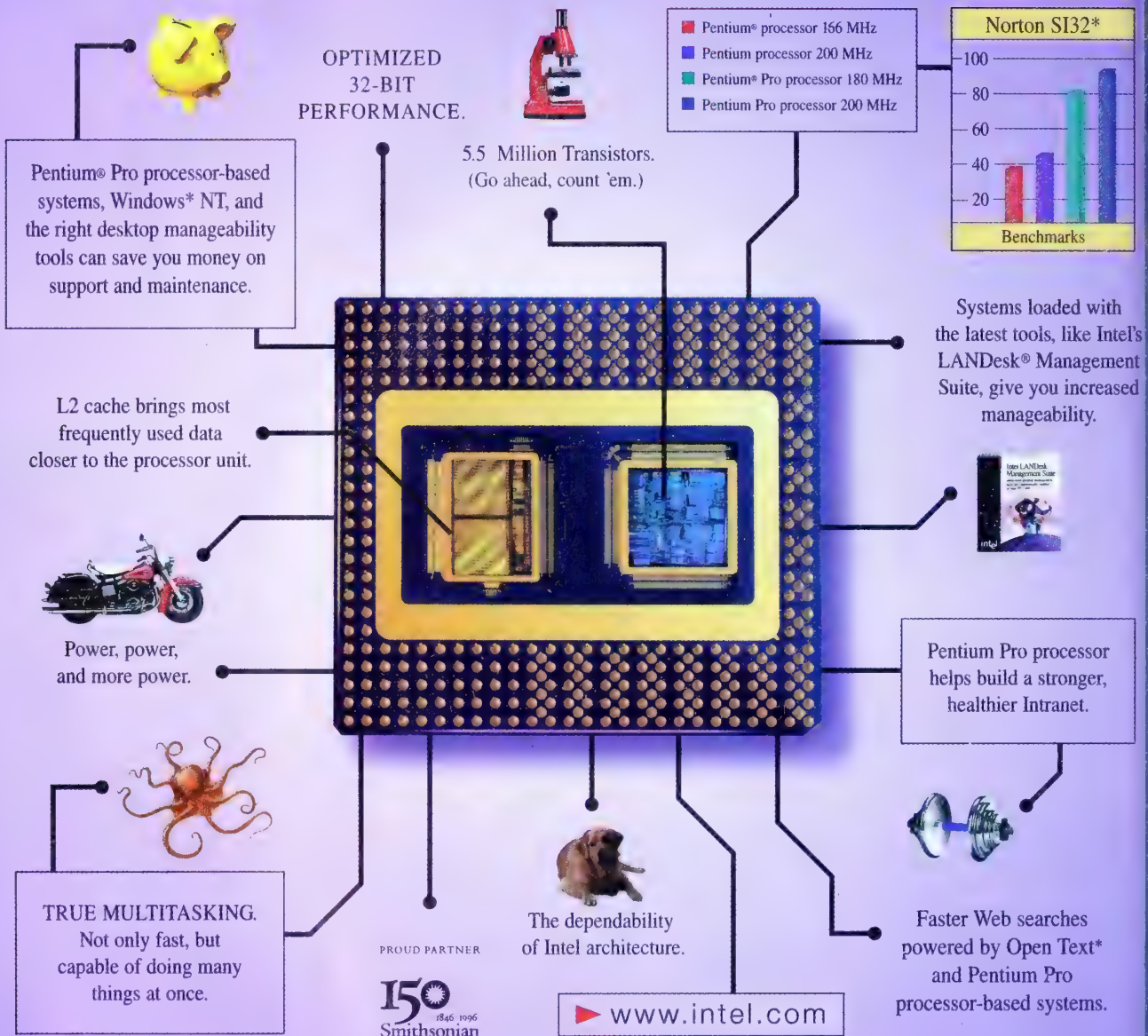
HUTOMO MANDALA PUTRA (Son, 34)

\$590 million

Kia Motor
Westinghouse Electric (planned)
NEC
Sumitomo
Rolls-Royce (agent)

DATA: INDONESIAN BUSINESS DATA CENTER AND BUSINESS WEEK

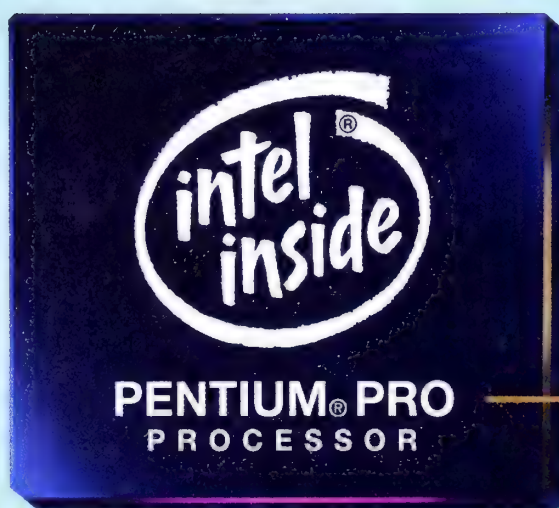
{ IT Overview }



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or as a loan that is paid off after the project starts earning profits.

Take the government's 1989 decision to allow foreign companies to add new phone lines in Jakarta. One contract went to NEC and Sumitomo, which were tied up with Tommy. Switch manufacturing contracts went to a joint venture with NEC and a second tie-up between AT&T and Tutut. Although Tutut is the chairwoman and has a 25% stake in the venture, now affiliated with AT&T

plier Batu Hitam Perkasa, which has a 15% stake. Shareholders of the coal supplier include daughter Siti Hedijati Hariyadi ("Titiek") and her brother-in-law Hashim Djojohadikusmo. In turn, Batu Hitam owns 15% of the plant but didn't put in its own capital. Instead, its share of the equity in Paiton is a loan to be repaid from profits. "In Indonesia, how the practice usually works is you lend the Indonesians their equity," says an investor close to the deal.

relationships with local partners." Morgan Stanley & Co., which was negotiating a joint venture with Tutut-affiliated Makindo, got second prize by being named adviser to Telkom.

SHAPING UP. Morgan Stanley doesn't deny that Tutut's name improves chances in business. But its executives insist there are more reasons than just the name. "Makindo is the prime joint venture opportunity in investment banking," says Ronald G. Felt, Morgan Stanley's executive director in Indonesia. "Everyone else is second-tier." Besides, Tutut isn't getting something for nothing, say sources familiar with the deal: She agreed to invest \$1 million in cash for her share of the joint venture's \$5 million equity. Merrill Lynch says the joint venture was required by Indonesian law.

Of all the children's companies, the one most recognized for professionalizing itself is Bambang's Bimantara. This year, profits are expected to rise 27%, to \$8 million, on sales of \$377 million. Management denies it has gotten a free ride on Bambang's ties. Finance director A. Kadir Assegaf says the company has assets worth \$3.3 billion and "plenty of cash flow." Assegaf: "After Mr. Suharto is no longer President, we can prove we are like any other private company."

The question for foreign investors involved in these deals is how to navigate their way through the transition, especially if the turmoil in Jakarta's streets

escalates. "If companies are seen to be contributing to the corruption in the country, they will be held liable," warns Laksamana Sukardi, a consultant who supports opposition leader Megawati.

It's a process that has already played out across Asia, where sudden changes of governments have led to the undoing of big-ticket deals ranging from nuclear plants and F-16 jet fighters to mass transit systems. As Suharto takes even harsher measures to control the frustrations spilling out into Jakarta's streets, domestic and foreign businessmen alike may start reassessing the stability they had long taken for granted.

By Pete Engardio and Michael Shuman in Jakarta, with bureau reports



spin-off company Lucent, she is not active in management and has contributed no capital, according to a source close to the deal. Lucent officials were not available for comment.

PROTECTION. Having a government official's children as deal partners isn't illegal under U.S. law. In some cases, the children bring real value. Hughes, for example, has a 10% stake in a satellite-communications venture with Bambang, called Pasifik Satelit Nusantara (PSN), and sells satellites to another Bambang-linked company, Satelit Palapa Indonesia (Satelindo). "We have no problem operating in that mode," says George A. Tadler, vice-president for Indonesian business development at Hughes Space & Communications International Inc. "It isn't bad to have a President's son as partner."

But in other cases, a clan member merely lends protection to a deal. Consider the construction of the \$2.5 billion Paiton power plant. One of the partners with General Electric Co. and Edison Mission Energy Co. is coal sup-

"That of course raises the cost." GE and Edison officials say they are small participants and the financing is above-board.

The frustrations of operating without powerful connections were driven home to executives of Salomon Brothers Inc. They're convinced they failed to win a 1995 deal to underwrite the \$1.7 billion listing of the government-owned phone giant, Telekomunikasi Indonesia (Telkom), because they tried to go it alone. Foreign brokers who participated in the bidding say the criteria were mystifying until a group of Wall Street banks led by Merrill Lynch & Co. won. It just so happened that Merrill Lynch was negotiating a joint venture with a company owned by Hashim and Titiek. "Salomon Brothers and the other [losing] brokerages were naive," recalls Gunawan Jusuf, managing director of the Makindo brokerage house. "They didn't think they had to bother building up solid re-

WINNING ENTRY

When Suharto's son Bambang sealed a pact with Hyundai to make the Cakra, America's Big Three found they were out in the cold

By Jonathan Moore

TAIWAN: OPEN THE TRADING DOOR TO CHINA, NOW

For the 44,000 residents of the parched island of Kinmen, also known as Quemoy, brown tap water dirtied by silt is an unhappy fact of life. The tiny Taiwanese-controlled outpost, just 2.3 kilometers from the Chinese coast, is famous as the target of shelling for decades after the Communist takeover of the mainland in 1949. Without access to the lakes and rivers of China's Fujian province, Kinmen's citizens rely on tankers to ship in water from Taiwan, over 200 kilometers away.

If Hsu Shiang-chen has his way, that won't be necessary much longer. Hsu, director of water resources at Taiwan's Economics Ministry, is supporting a plan drafted by the governments of Kinmen and Fujian to pipe in drinking water from China. As relations improve, the idea is not as far-fetched as it might seem. "We are very interested in this plan," Hsu says.

The fact that some Taiwan officials are studying such a proposal shows how far they have come since the tensions of last March. But there's a big hitch: China and Taiwan must first agree to direct trade before the water could start flowing to Kinmen. Because of Taipei's longtime ban on direct business with the mainland, trade and investment are carried out indirectly, mostly through Hong Kong. But since the British colony reverts to Chinese rule next year, Taipei officials are under pressure from the business community to revise their laws. At the same time, politicians from both the ruling and opposition parties fear that to open up direct trade is to fall into a trap set by Beijing to ensnare Taiwan.

DEATH GRIP. Taiwan's President Lee Teng-hui should simply accept the inevitable and launch a new era of direct trade with China. Taiwanese need to start building confidence that they can trade directly with China without being swallowed by it. The

best insurance against the economic death grip that Taipei fears from Beijing is an internationalized economy with strong ties to world financial markets. With so many Taiwanese industries relocated in China, Taiwan's capital, technology, and managerial talent make a perfect match for China's huge market and inexpensive land and labor. Taking greater advantage of those ties would help make

will be protected. Without it, Taiwan's leaders fear Beijing would use economic ties to pressure them to accept its idea of "one China." Local governments in Fujian, for instance, may be keen for closer economic ties with Taiwan, but Beijing sees direct links more as a political club to promote unification on its terms.

ECONOMIC ZONES. Aware of Beijing's motives, Taiwan's government has

been buying time, floating creative measures to get around its own ban. Beijing has already vetoed an idea to make Taiwan's ports into "offshore" transshipment centers allowing foreign-flag vessels to ship goods directly between Taiwan and China. That hasn't stopped Taipei policymakers from discussing a similar proposal to create special economic zones in Taiwan that could trade directly with China. After next July 1, Taipei will continue to treat Hong Kong as if it weren't part of China. Given Taiwan's willingness to consider quasi-direct trade, the government should be willing to realize that it can do business with the mainland without sac-

rificing its de facto independence. Taipei and Beijing are taking some steps toward improved ties. Officials are approving larger investments by Taiwanese companies in China and have even allowed Taiwan's state-owned oil company to explore for oil and gas with Beijing's state oil company. In July, Chinese shipping, telecommunications, and securities delegations held unofficial talks with Taiwan counterparts about economic cooperation. But at that pace, the people of Kinmen will have to wait far too long before they can get a clean glass of water.

Moore is BUSINESS WEEK's Taipei correspondent.



Taiwan more of a global economic force.

Taiwan can't afford to delay. Its companies have committed some \$25 billion to indirect investments in China, and larger investments are pouring in steadily. These ties will continue with or without direct links. Meanwhile, direct trade would help Taiwan generate the economic strength it needs to resist Beijing. Taiwan's companies would gain from closer ties with China. Moreover, direct trade and air flights would become the key selling point for Taiwan's plan to become a regional hub for multinational businesses. That would hasten Taiwan's internationalization. If Taiwan waits too long or tries to go its own way, it risks being marginalized. "An independent Taiwan may be faced with a Cuba-like economic isolation," says Peter Kurz, Taiwan branch manager of ING Baring Securities Ltd.

Before it allows direct trade, Taipei wants a guarantee that the island's sovereignty and way of life

CHEERS

Shipping executives from China hold unofficial talks with Taiwan business leaders on forging economic ties

TWILIGHT OF THE GODS

A scandal touching Italy's Big Three signals the end of an era

The ground is shifting beneath Italy's two most hallowed business behemoths. At Fiat, 75-year-old patriarch and former Chairman Gianni Agnelli is recuperating from heart surgery. Fiat's current chairman, Cesare Romiti, will himself step down when he turns 75 in 22 months. And at Mediobanca, the Milan merchant bank that acts as Fiat's financial backbone, the career of 88-year-old Honorary Chairman Enrico Cuccia is drawing to a close. "The Big Three of

ciala say they will not comment publicly on the investigation.

Indeed, the changes that shook up Italy's political old guard are now sweeping through the business world. Big companies, which often managed multimillion-dollar slush funds, have largely cleaned up their acts. Foreign investment banks and pension funds are more active than ever on the Milan bourse, insisting on transparency. And privatizations, such as the projected sell-

merger was announced, Gemina stunned the market with news of massive, explained losses at its Rizzoli publishing unit. Only days before, Gemina management had painted a rosy picture of a turnaround at Rizzoli. Gemina shares, essential to securing the merger's cash stock swap, plunged in value as investors bailed out.

Soon afterward, Italy's tax police raided Gemina's neo-Renaissance headquarters in central Milan. That afternoon, prosecutors said that 10 top Gemina managers were under investigation on charges of falsifying company balance sheets to hide losses. Thousands seized documents provided fodder for the broader upcoming investigation, to Cuccia's master plan was history.

It was a defeat for Cuccia—and an embarrassment for Maurizio Romiti, Cesare's son and a top Mediobanca official who oversees Gemina's business within the bank. "The Gemina affair is a great loss of credibility for Mediobanca and is the beginning of the end of the system it has ruled over," says Salvatore Bragantini, head of Milan-based merchant bank Arca Merchant.

The bad news from Gemina seemed endless. In late June, management announced revised consolidated 1995 losses of \$464 million, way beyond the \$23 million in losses it had forecast last November. And the scandal could affect the relationship between Romiti and Agnelli. Although the two men publicly deny any rift, Romiti and Agnelli recently broke ranks in public. In June, Romiti declared that family capitalism in Italy was ending. That brought an immediate public rebuke from Agnelli, who warned Romiti to keep focused on Fiat and not get caught up in Italian politics.

FRESH FACE. Observers say Agnelli may be trying to reassert family control at Fiat. But even if the Agnellis win the power struggle for Fiat's future, the new management style won't look like the old. In June, Gianni Agnelli pushed through the appointment to Fiat's board of Paolo Fresco, General Electric Co. Italian-born vice-chairman. Insiders say the Agnellis want Fresco to replace Romiti as Fiat's chairman in 1998, when Fresco turns 65 and must resign from GE. Waiting in the wings: Giovanni Agnelli, Gianni's nephew.

Fresco's appointment would show that Italy's business culture is indeed changing. "Fresco may know nothing about cars," says one banker close to the Agnellis, "but he's totally new, totally clean, and has had no involvement with the past." Considering the stock of Gemina, those may be the most important credentials the next generation of Italian business leaders can have.

By John Rossant in Rome

Italy's Old Guard and Its Network



GEMINA

Troubled conglomerate with \$900 million in sales and big stakes in publishing, banking, fashion, etc. Maintains close management ties with Mediobanca and Fiat. Facing criminal investigation for false accounting.



ENRICO CUCCIA

FIAT

Auto giant, presided over by patriarch Gianni Agnelli, owns 42% of Gemina's controlling shareholders' syndicate and 2% of Mediobanca. Chairman Cesare Romiti has strong influence over Gemina strategy.



CESARE ROMITI

MEDIOBANCA

Premier merchant bank, with stakes in Italian finance and industry, including 2% of Fiat. Top executive Maurizio Romiti, son of Cesare and possible successor to Mediobanca's Enrico Cuccia, could suffer from ties to Gemina.

Italy are leaving the scene," says a former Fiat top executive. "And that means uncertainty, because no one enjoys anywhere near their authority."

In a country where family control of businesses is more personal than anywhere else in Europe, generational change at Fiat and Mediobanca is bound to cause unease. But the passing of the baton could also be tainted with scandal. Gemina, the Milanese holding company in which Fiat and Mediobanca have long been key players, faces potential criminal charges for irregularities that could include falsified balance sheets, tax evasion, and insider trading. Gemina offi-

off next February of state-owned telecommunications giant Stet, stand to create new centers of corporate power.

Neither Fiat nor Mediobanca will comment on the Gemina scandal until the investigation is complete. And although indictments seem highly likely, Agnelli, Romiti, and Cuccia will probably not be touched directly by them. But the Gemina affair has already inflicted damage. For example, last September Cuccia announced an ambitious plan to create a new \$24 billion industrial group by merging nine public companies controlled by Fiat and Montedison. But barely three weeks after the

EDITED BY DOUGLAS HARBRECHT

CHINA: WHY THE U.S. WANTS TO PLAY 'LET'S MAKE A DEAL'

With the clouds lifting over the troubled U.S.-China relationship, a breakthrough may be near. The Clinton Administration is quietly signaling Beijing that the U.S. is ready to end the stalemate blocking Chinese membership in the World Trade Organization. The Administration wants China to agree to stiff commercial conditions before it can enter the new global trade club. But for the first time, the U.S. is willing to haggle over terms—and it's ready to be flexible. Already, U.S. policymakers are offering a negotiating centerpiece that Beijing craves: permanent most-favored-nation trade status. National Security Adviser Anthony Lake privately outlined the shift in policy in talks with Chinese leaders in Beijing. Next month, Acting U.S. Trade Representative Charlene Barshefsky and Commerce Secretary Mickey Kantor will reinforce that message when they meet with Yi, China's Trade Minister, in Beijing. To avoid any partisan wrangling, the real bargaining won't begin until after the November Presidential election. But Administration officials aim to cut a deal with Beijing on trade entry early in 1997.

TRADING PROTECTION. The outlines of a possible agreement are starting to emerge. Washington will insist that China eliminate tariffs, quotas, and licenses on a slew of goods; provide access to key U.S. service sectors such as telecommunications and insurance; and end rules that force foreign companies to do business through Chinese intermediaries. China would get permanent MFN and gradual phaseouts of subsidies for state-owned enterprises, plus special protection for sensitive sectors such as autos and machinery. What's driving the U.S. to jumpstart moribund WTO negotiations? Administration officials figure they have much to lose. "There's a growing awareness that China's economy will soon be too big to shut out of the world trading system," says one Administration Asia hand. Once in the WTO, Beijing would be obliged to play by international rules—be subject to international sanctions for noncompliance. U.S. officials know that the Chinese see WTO accession as a litmus test of America's commitment to a stable Sino-U.S. relationship.

Striking a deal would also get the U.S. off a treadmill of fighting nasty bilateral battles for piecemeal trade gains. Instead of repeatedly threatening sanctions to force concessions, Washington could wrap most spats with China into multilateral negotiation. That would give the U.S. a better shot at mustering up support in Europe and Japan for

its aims while minimizing Beijing's ability to play the U.S. off of its trading partners by steering contracts to foreign business rivals.

The economic imperative to rev up WTO talks dovetails with a crucial shift in sentiment on Capitol Hill. Influential lawmakers such as Representatives Doug Bereuter (R-Neb.), chair of the House Asia subcommittee on international relations, and Bill Archer (R-Tex.), chair of the House Ways & Means Committee, are quietly mulling ways to end annual debates over MFN for China. They and other Hill free-traders are weary of the yearly China-bashing in Congress.

Sounds easy. But achieving an agreement will be anything but. The lure of permanent MFN may not be enough in itself to get China to agree to conditions the U.S. regards as must-haves. The Chinese view normal trade privileges as their due. "MFN isn't really too much of a bargaining chip," scoffs Fan Gang, director of the China Reform Foundation in Beijing. "Chinese officials know the U.S. will give it to them anyway."

Beijing is sure to insist on special treatment for emerging Chinese industries. Already, there are growing calls inside the Middle Kingdom to shield beer, chemicals, and consumer electrical goods companies. Such a din will make negotiating conditions for WTO entry extremely contentious. "We're trying to integrate the biggest nonmarket economy into the global trading system. It will probably be the most difficult trade negotiation the U.S. has ever tried," warns Greg Mastel of the Economic Strategy Institute.

Even if both sides strike a bargain, Congress could still spoil the deal. Lawmakers may balk at ending the legal requirement for the President to re-

view China's MFN status each year, especially with Hong Kong's reversion to Chinese control looming next July 1. U.S. officials already are sweating over plans by House Minority Leader Richard A. Gephardt (D-Mo.) to introduce a bill this fall that would give Congress veto power over any WTO deal. A yeay vote may be hard to resist—there's no love lost for the WTO, which many lawmakers view as intrusive on U.S. sovereignty.

There are plenty of risks. But the Clinton Administration is determined to forge ahead. The potential benefits of securing China's commitment to abide by established rules are too alluring.

By Amy Borrus in Washington, with Dexter Roberts in Beijing



MAKE ME AN OFFER

Acting U.S. Trade Representative Charlene Barshefsky will dangle permanent most-favored-nation status as a way to get China to make concessions

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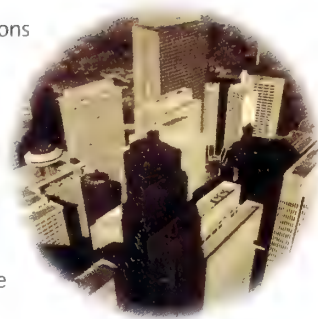
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HE'S A ONE-MAN RADIO BAND

Bob Sillerman plays so many roles, investors are dizzy

Robert F. X. Sillerman has a framed photograph prominently featured in his midtown Manhattan office. It's of him, nude, in a bathtub with his young daughter. There's nothing wrong with the display, exactly, but there's something not quite right about it, either.

The same could be said for the way Sillerman runs the three publicly traded radio companies—SFX Broadcasting, Multi-Market Radio (MMR), and Triathlon Broadcasting—that he either controls outright or advises while holding a huge nonvoting stake. All told, Sillerman oversees more than 100 radio stations, making him one of the largest radio honchos in the country. But as he has assembled his growing empire, he has engaged in some practices that have brought sharp criticism from shareholders and Wall Street. A close reading of the companies' public filings shows that Sillerman has long acted as each company's investment banker, financial adviser, chief strategist—and even landlord. And he has collected fees for wearing each hat.

Sillerman "has clearly had his fingers in more than one pie for years," says CS First Boston analyst Harry DeMott. "One could argue there's nothing wrong with that, per se. A company has to pay someone a fee as an investment banker or broker. But it sent the wrong message to the market." Retorts Sillerman: "If they [don't] like it, they can sell."

Indeed, despite a



runup in the value of SFX and almost all radio stocks, thanks to telecom deregulation, SFX still trades at a significant discount to its peers (chart). MMR stock trades at an even sharper discount, while Triathlon shares have fallen 28%, to 8¢ in the past six months. The poor performance galls Sillerman, who boasts that given the multiples others have paid in recent months to acquire Infinity Broadcasting and American Radio Systems, SFX is "over a \$100 stock." As the largest shareholder, he stands to gain more than anyone from such a surge.

But Sillerman has not waited for the wider market to hand him his payoff. Although he draws a healthy salary as

chairman of SFX—\$300,000, plus options in the past three years on 220,000 shares already worth \$5.8 million—he has pocketed millions in fees through privately held Sillerman Communications Management Corp. (SCMC).

The 48-year-old tycoon vows that loyalty lies with SFX, the only company he serves as an executive, and its shareholders. SFX, which had 1995 revenue of \$76.8 million, has grown from 17 stations to more than 70 stations in markets such as San Diego, Charlotte, NC, and Nashville since it began an acquisition

binge last fall. Sillerman, through SCMC, has acted as investment banker and broker on all those acquisitions. He pocketed \$4 million in such fees for two recent deals.

POOL OF ASSETS

Sillerman's management company collects millions in fees from his radio empire

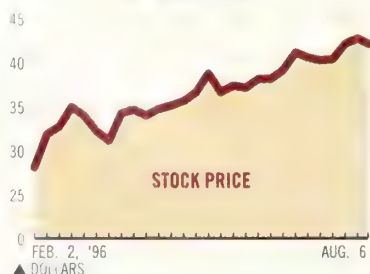
and an additional \$2 million for SFX pending merger with MMR—a company Sillerman also founded and controls. The fees were approved by SFX's six-member board, which includes two outsiders.

RED FLAG. But that's not the end of Sillerman's gravy train. SCMC's 10-year consulting contract with Triathlon pays \$466,000 a year. On top of that, SCMC collected \$1.5 million in fees from Triathlon in the past year for finding acquisition candidates, negotiating agreements, and setting up a preferred stock offering. The tiny San Diego-based Triathlon had revenues of only \$3.5 million for the year ended Mar. 31. Even though Triathlon stations compete against

SFX stations in Wichita and the two companies could potentially want to buy the same stations while Sillerman acts as the broker and investment banker for each, Sillerman says there is no conflict. "Somebody should not be involved in Triathlon unless they believe that we are people of integrity," he says.

In partial recognition

SFX'S STOCK IS WAY UP...



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RATIO OF CURRENT SHARE PRICE TO PROJECTED 1996 OPERATING CASH FLOW

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CHANCELLOR	16.2
EMMIS	14.6
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of the drag such fees place on the stock of all the companies, Sillerman has agreed as part of the MMR merger to eliminate the fees SCMC draws from SFX. In return, he pocketed stock warrants already worth \$5.9 million and doesn't have to repay a \$2.2 million loan from SFX. Triathlon will still pay its fees to SCMC, but SCMC will hand those fees over to SFX. One institutional shareholder who met with Sillerman to complain about the arrangement in early June didn't get very far. "His response was, 'What's wrong with you? The stock is up, so why do you care?'" says the miffed shareholder. Sillerman says he is responsive to shareholder complaints.

DEBT-HEAVY. He got into radio in 1979, when he and his partner, New York deejay Bruce "Cousin Brucie" Morrow, bought a radio station in upstate New York. Sillerman says he did everything at the station from the "janitorial work to hanging the curtains" as he learned the business. Over the years, he and Morrow bought more radio stations, a few television stations, and launched Country Music Television. In 1989, he sold most of his holdings to Westinghouse Electric Corp.'s broadcasting division for \$720 million and started again. He took SFX and MMR public in 1993, and Triathlon public last year. Except for SFX in 1994, none of the debt-heavy companies has ever posted a profit. "Earnings are not what we're currently interested in," says Sillerman, who plans to use debt to finance new acquisitions.

A likely acquisition candidate for SFX is Triathlon. SFX's habit of acquiring properties in which Sillerman already has a financial interest won't do anything to goose SFX's share price, says another big shareholder. SFX is in larger markets, while MMR is in small Eastern markets, and Triathlon is in small Western ones. "Each time Sillerman [has SFX buy one of his other companies], SFX becomes less focused and less attractive" to another radio company that might want to acquire SFX, the shareholder says.

But there are insider deals even Sillerman can't stomach. This spring, SFX said CEO Steven R. Hicks would leave to start a rival radio group with his brother, Thomas O. Hicks of Dallas-based Hicks, Muse, Tate & Furst Inc. Hicks, who was to remain a director with a five-year, \$150,000 consulting fee, left in June without his board seat or consulting contract.

Why? Having him as a consultant and director, privy to SFX's strategy, would be unseemly, says Sillerman, since Hicks is now a competitor. "That was fraught with conflicts and the appearance of conflict," he says. "He's out there investing. Just imagine." An odd arrangement, to be sure. But not unheard of.

By Elizabeth Lesly in New York

The Corporation

«STRATEGIES»

KINKO'S GOES CORPORATE

With buyout firm CD&R on board, the hard-back chain of copy shops is headed toward an IPO



The mood was buoyant as the partners and store managers of Kinko's Inc. arrived in San Diego for the company's 26th annual meeting and picnic on July 11. As always, the attendees heard presentations, watched skits, and applauded employees cited for creative ideas. But this year, there would be something new: outsiders.

As Chairman Paul Orfalea introduced bankers from New York buyout firm Clayton, Dubilier & Rice Inc.—which on June 10 announced plans to take a 30% stake in Kinko's for \$200 million—employees applauded loudly. Still, they knew the deal would forever change the copy-shop chain, based in Ventura, Calif., from a quirky, loosely managed group of private partnerships to a more buttoned-down company on the road to an initial public offering. Joked Tim Stancliffe, a longtime Kinko's partner: "Back in my college days, I would have called [CD&R] the *crème de la crème* of the capitalist-pig insect world. Now that I want their money, they're savvy."

The transition from counterculture casual to mainstream mature is one few Kinko's managers thought they would ever have to make. Under Orfalea, who founded Kinko's in 1970 with one copier in a converted taco stand, the privately held company grew—without outside

help—into the country's largest chain of 24-hour photocopying stores. Orfalea created an unorthodox structure, forming a separate partnership in each market Kinko's entered—all 128 of them. Decisions were made by consensus, and even store clerks had a say. **GROWING PAINS.** For years, the system worked. Today, Kinko's has 851 stores—18 of them overseas—and holds an estimated 25% to 30% share of the \$5 billion to \$6 billion retail copy market, says Prudential Securities Inc. analyst Alex Henderson. The company doesn't disclose its financials.

But mounting competition, rising costs, and the constrictions of Kinko's management structure have caused growing pains and hurt profits. Orfalea concluded that Kinko's needed help to profitably expand its customer base beyond students and entrepreneurs to national businesses with sophisticated technology needs. So Orfalea interviewed some 15 investment firms last year, finally choosing CD&R for its probing questions. The investment firm will centralize Kinko's partnership structure, help choose outside managers, and bankroll the company's plan to reach 2,000 stores by 2000. Orfalea, 48, nicknamed Kinko for his curly red hair, says the decision reminded him of his wedding day. "It's scary and happy at the



ne time," he says, "but it's the right time to do."

Duplicating Kinko's early successes will be tough for CD&R. Thanks to its near-monopoly position in the college market, Kinko's grew rapidly, financed

Orfalea and his partners, who owned shares of their own stores. Orfalea put a premium on rewarding innovation. One example: Each year, employees of the store with the best new idea—this year, a user's guide to Kinko's computer stations—win an all-expenses paid vacation to Disneyland or Walt Disney World. Kinko's board—Orfalea included—stays behind to man the counters.

CROWDED FIELD. Yet as Kinko's became a national powerhouse, the structure became unwieldy. Expansion was uneven, with strong partnerships making the best of their markets while weaker operations sometimes didn't open enough stores. And the consensus-based style meant that Orfalea spent much of his time haggling over niggling details. After losing a 1989 copyright-infringement suit over the reproduction of texts, Kinko's stepped up its move toward its new target: small and self-employed businesspeople who couldn't afford high-tech equipment but needed premium services such as color copying. Yet it's a crowded field, full of franchisers such as Quick Copy and Sir Speedy Inc. Now, compa-

nies such as OfficeMax and Office Depot are expanding copy services.

The competition has squeezed profits across the board. According to the National Association of Quick Printers, the industry's average net profit margin fell from 17.9% in 1983 to 13.6% in 1995, driving many mom-and-pop shops out of business. Most of Kinko's sales still come from low-margin photocopying services, and the availability of cheap laser printers that can provide high-quality copying at home is eating into that business. At the same time, Donald J. Gogel, co-president of CD&R, says it's now three times more expensive to open a Kinko's than it was just five years ago. That's because of rising labor costs and the costlier new technology needed to reach Kinko's expanded target market. It's also one reason some 30% of Kinko's stores aren't profitable.

To get Kinko's printing more profits, CD&R will centralize operations. This will help Kinko's save on purchasing and cut

Now outsiders will bankroll expansion at the outfit founded in 1970 in a converted taco stand

"SCARY AND HAPPY": ORFALEA AT THE COMPANY PICNIC

interest costs by \$20 million to \$30 million as partners' debts—now often personally collateralized—are consolidated. CD&R's capital will also be used to expand overseas and interconnect all the Kinko's stores.

The linkup will help Kinko's compete in digital electronic imaging, a new market that Prudential's Henderson thinks will grow 50% a year. This service, still less than one-half of 1% of industry sales, lets customers send in information electronically, which Kinko's can then print out anywhere, anytime. A business traveler, for example, might send documents over the Internet to Kinko's in Las Vegas, San Francisco, and Tokyo for pickup at a later date. Yet investing big bucks in high tech brings risks. Videoconferencing, introduced in 1995, is a smash with New York ad executives, but the equipment is rarely used in Ventura stores.

In the meantime, Kinko's is pursuing large customers, such as Wyeth-Ayerst, the \$8 billion pharmaceuti-

cal division of American Home Products Corp. In January, Jackie Franke, purchasing manager for Wyeth-Ayerst, opened a national account for her 3,000 traveling salespeople. They've spent \$200,000 on jobs so far. "Everyone's been happy," she says, noting she chose Kinko's for its reach. "The more stores they open, the better."

IDEA MAN. To make the plan work, Kinko's is counting on CD&R's seasoned management—led by partners Gogel and Andrall E. "Andy" Pearson. Gogel successfully reshaped IBM's \$1.6 billion typewriter business into \$2 billion printer maker Lexmark International Inc., and Pearson, the ex-president of PepsiCo Inc., won kudos for the company's success in foods. But the key to success will be keeping Orfalea happy. With approximately 34% ownership of the new Kinko's—conservatively valued at \$226 million—he will be the largest shareholder and a board member. Still, he has no official title and says vaguely

that he will be the idea man, working on such new concepts as airport kiosks.

For its \$200 million, CD&R gets about 30% of the company, 6 of 11 board seats, and veto power over the company's soon-to-be-

named CEO and CFO. The partners will be folded into one group owning one-third of the company, and the estimated 3% who want to be bought out by CD&R will be paid out of a \$75 million fund. Most should stay, charmed by the prospect of striking gold when the company eventually goes public. "CD&R likes to invest where there's strong opportunity," says Lloyd Grief, a Los Angeles investment banker. "This will be a sweet deal."

Still, no one thinks the shift will be free of snags. "There will be turmoil in the transition," admits Tom Parrish, a board member who started at Kinko's as a clerk. Dennis Itule, Orfalea's cousin and one of the first Kinko's partners, says he went through a mourning period after the change was announced. "Once in a while you have a twinge," he says. "But the other side is, we can gain a lot." If CD&R can reproduce the Kinko's magic, it's a sacrifice worth making.

*By Nanette Byrnes
in San Diego*

How Kinko's Will Iron Out Its Kinks

- Select an outside CEO and CFO; centralize the unwieldy partnership structure
- Invest \$200 million in new technology and stores in the U.S. and abroad
- Pursue large business customers with its national presence and improved service

Why he can look forward as he would have a cen

Today, no one thinks twice about somebody living to the ripe old age of 80. A hundred years ago, however, it was a rarity.

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STOCKS

IPOs: A SUMMER OF DISCONTENT

A sour market, product flops, all made for a bad ride

Just a few weeks ago, investors and market mavens were writing the epitaph for the bull market, kissing off everything from the rock-solid blue chips down to the most speculative initial public offerings. But in a remarkable turn, the Dow Jones industrial average has piled up some 370 points since last month's low, and even the tech-laden NASDAQ Composite Index has climbed 9.5% from its bottom. In the IPO market, however, you can still hear the chisels chipping away on the gravestones.

Pity the poor investor who got sucked into the euphoria of the once surging IPO market of 1996. The Standard & Poor's New Issues Index, which measures the first six months of IPOs' performances, jumped 41% from January to mid-May and has now dropped 20% from that peak. Sure, the average return for the 436 members of this year's IPO class is 10.5%, according to Securities Data Co. But that's based on the difference between the IPO price and the market price on Aug. 2. Most new offerings initially traded much higher, so most investors paid a lot more.

THAT'S HIGH-TECH. Indeed, behind the averages, the damage is worse (table). Look at Yahoo! Corp., the Internet search engine company. It was taken public by the prestigious Goldman, Sachs & Co. at 13, shot up that day to 43 and now sells at 18, down 57.9% from its peak. Heck, that's high-tech. Consider Garden Botanika Inc., a cosmetics retailer backed by Montgomery Securities. Issued at 20, the stock ran up to 35. Now, it's at 16. "IPOs are the leading edge of risk," says Robert Natale, editor of *Standard & Poor's Emerging & Special Situations*, which reports on IPOs.

The investment banks, which made a bundle taking companies public, are also feeling the pain. Compared with the supercharged activity last spring, the new-issues market is as flat as yes-

terday's soda pop. The pace of new offerings has been cut in half. The prices at which they're done have been slashed. On Aug. 6, jeans maker Guess Inc. cut its asking price for its IPO by 13% and reduced the number of shares by 24%. Aftermarket performance is flagging, too. "Before, a hot deal could double

the first day," says George S. Shirer, a researcher for the newsletter *New Issues*. "Now, you're lucky to see 20%."

An IPO revival is still not in sight. Among the big investors that buy the stocks, "there's reluctance and resistance to talking about new names," says David H. MacCallum, head of life sciences investment banking at UBS Securities Inc. Part of that is caused by market skittishness, and part the fact that mutual-fund managers in particular have relatively little to spend. Cash levels are low, and inflows to funds as much as \$1 billion a day a few months ago, are estimated to be \$3.5 billion all of July.

JITTERS. The investment banks use the initial offering price as a benchmark to measure the performance of their IPOs. Using that gauge, Donaldson, Lufkin & Jenrette Securities Corp. has this year's best record among the major underwriters. Its 15 deals are up an average of 23.1% over their opening price, and more important, only two are trading below it. Hambrecht & Quist, which is pioneering its own IPO in August, has an average of 21.3%, although 7 of its 16 deals are trading below their initial price. At the other extreme, there's Dillon, Read & Co., whose six deals are down an average of 24.6%, and UBS Securities, down 34%. UBS's MacCallum says his firm's results are low because five are biotech and medical-device companies, which have been hit among the hardest in the IPO rout. Dillon, Read did not respond to requests for comment.

True, the underwriters can't be held responsible for a price decline that sweeps through the market because of, say, inflation or interest-rate jitters. But they can be taken to task when price declines come from problems with the companies they backed. Few investment banks haven't suffered some embarrassing "blowup." That's when a newly minted company blows its first or second earnings report, a major product flop, or a key executive bolts. The due diligence for IPOs is more rigorous than for established companies, notes Sanford R. Robertson, chairman of Robertson, Stephens & Co., "when one blows up, it really reflects on your [investment] banking."

No one at Oppenheimer & Co. would comment about Dignity Partners Inc.



ght public in February at 12. Dignity purchases life-insurance policies of terminally ill, mostly AIDS suffer- giving them cash to use while re still alive. But good news for victims—the recent International erence on AIDS reported that with therapies, many can live with the use—was deadly for investors. On 16, Dignity halted purchases of policies, and the shares plunged. are now 75% down from their Dignity did not return calls.

Another one of the year's worst ups is Cerion Technologies Inc., a manufacturer of magnetic thin film disks in computer drives. The company public on May 24 at 13 and traded high as 19%. Cerion started falling une, along with the other tech cs. But on July 9, Cerion announced its largest customer, accounting for of sales, had canceled all its or- . The stock collapsed and now sells James P. Hickey, a principal at iam Blair & Co., Cerion's under- er, says the prospectus listed the ndence on a few large customers he stock's No. 1 risk. Still, "it's emendous disappointment," says ey. "We got a lot of flack from stors."

ORDABLE. The bright spot in the IPO cle is that the prices are lower— there are fewer investors bidding shares. James "Chip" Roberts, a folio manager at Oberweis Emerg- Growth Fund, says he has been able uy stock in two companies in re- weeks that three months ago he ld have had to pass up. Both comes, Multiple Zones International Inc., ch sells computers and software by log, and Research Engineers Inc., ch designs software, went public at es below what issuers first sought. Investment bankers have also tried to up the market-mauled IPOs, arguing the companies are still sound. John Skeen, research director at Mont- ury, says that of his firm's 20 IPO ls this year, there are only four in ch the fundamentals have changed the worse. One chief of investment king at a major underwriter recalls as'n't that long ago, the summer of 4, "when you couldn't give away se [IPO] stocks." Since then, the S&P w Issues Index has risen 133%, even nting the recent sell-off.

Three weeks ago, you couldn't give ay blue chips, and now investors are noring for them. It will take more n three weeks, but investors have rt memories. Before long, they'll like- be clamoring for IPOs as well.

By Jeffrey M. Laderman in New k, with Linda Himelstein in San ncisco

The Worst of the IPO Class of '96

COMPANY	LEAD UNDERWRITER	PRICE			% CHANGE FROM HIGH
		IPO	HIGH	RECENT	
AFFINITY TECH. GROUP	Montgomery Secs.	13	24½	6%	-71.6%
AKSYS	Smith Barney	16	23½	10%	-56.4
AMERICAN PORTABLE TEL.	Donaldson Lufkin	17	17%	10%	-43.0
ARTERIAL VASCULAR ENG.	Cowen	21	49½	22½	-54.0
ASPECT DEVELOPMENT	Alex. Brown	20	36½	25	-31.5
AUTONOMOUS TECH.	Hanifen Imhoff	8	8%	4%	-47.9
AVIGEN	Wedbush	8	13%	5%	-60.4
CARDIOGENESIS	Bear Stearns	20	23%	10%	-53.8
CARDIOTHORACIC SYSTEMS	UBS Securities	18	25%	12%	-51.0
CERION TECHNOLOGIES	William Blair	13	19%	4	-79.5
CHILDTIME LEARNING	William Blair	11	14%	7%	-45.6
COMPUSERVE	Goldman Sachs	30	35½	13½	-61.0
CONCEPTUS	UBS Securities	14	22%	9%	-59.3
CYLINK	Robertson Stephens	15	28%	12%	-56.1
DIGENE	UBS Securities	11½	12%	5%	-54.0
DIGNITY PARTNERS	Oppenheimer	12	14½	3%	-75.0
ECLIPSE SURGICAL TECH.	PaineWebber	16	19	7%	-59.2
ESC MEDICAL SYSTEMS	Smith Barney	15	46½	20%	-55.4
EXCITE	Robertson Stephens	17	21%	7%	-66.5
FLAMEL TECH.	Alex. Brown	7%	12%	7%	-36.7
GALAGEN	Montgomery Secs.	10	10%	5%	-50.0
GARDEN BOTANIKA	Montgomery Secs.	20	35	16	-54.3
GEOSCIENCE	Morgan-Keegan	17	20%	10%	-47.6
IMAGYN MEDICAL	Dillon Read	15	18	7%	-57.6
INDIVIDUAL	Robertson Stephens	14	24½	7%	-68.4
INFONAUTICS	Hambrecht & Quist	14	14½	7%	-50.9
INFOSEEK	Alex. Brown	12	16%	6%	-62.1
LOGAL EDUC. SOFTWARE	Lehman Bros.	8	8%	4%	-45.7
LYCOS	Hambrecht & Quist	16	29%	6%	-77.4
MICROCIDE PHARM.	Merrill Lynch	8	20%	10%	-47.6
NOVOSTE	Piper Jaffray	14	15½	9	-41.9
OPEN MARKET	Goldman Sachs	18	42¾	17%	-59.2
OPEN TEXT	Montgomery Secs.	15	26½	5%	-78.3
OPTICAL SENSORS	Alex. Brown	14	15%	6%	-56.5
OZEMAIL	Montgomery Secs.	14	17	9%	-44.1
PHYSIOMETRIX	Wheat First	11	12%	6	-52.9
PLANNING SCIENCES INTL.	Alex. Brown	16	32%	16%	-49.4
POWERCERV	Robertson Stephens	14	19½	4%	-75.0
PRISM SOLUTIONS	Alex. Brown	17	36%	15½	-57.8
RISCORP	Smith Barney	19	23%	13%	-42.4
SEGUE SOFTWARE	Alex. Brown	18	40%	10%	-73.5
SPRETRALINK	Robertson Stephens	8	12%	6%	-47.6
SSN&C TECHNOLOGIES	Alex. Brown	19	23%	9%	-61.2
VIRUS RESEARCH INST.	Oppenheimer	12	12%	6½	-46.9
VITALCOM	Wessels	12½	23%	9%	-59.0
VOCALTEC	Hambrecht & Quist	19	20%	6%	-70.5
WALSH INTERNATIONAL	J.P. Morgan	12	15%	9%	-41.1
YAHOO!	Goldman Sachs	13	43	18%	-57.9
XEIKON	Alex. Brown	15	27%	10	-64.1
XETEL	Prudential Secs.	8	10	5	-50.0

DATA: SECURITIES DATA CO., BLOOMBERG FINANCIAL MARKETS, BUSINESS WEEK

ARCHER-DANIELS' PAIN MAY BE INVESTORS' GAIN

Business is solid, despite legal problems sinking the stock

Long-suffering shareholders of Archer-Daniels-Midland Co., having endured embarrassing revelations of alleged corporate misconduct, are bracing for another trip to the woodshed. In September, the U.S. Justice Dept. expects to bring price-fixing charges involving the animal-feed ingredient lysine against ADM and two key executives. A month later, the grain and oilseed processor is likely to unveil weak earnings due to steep commodity prices. And on Oct. 17, reform activists are poised to vent complaints about corporate governance at ADM's annual meeting.

It's enough to make most investors run for cover. Although neither the company nor its executives has been charged with wrongdoing, the perception remains that ADM has a crooked streak. The stock badly lags the indexes (chart). ADM's basic businesses, though, remain sound. And ongoing corporate governance reforms spurred by the probe could strengthen the company further. If ADM stock gets beaten down more, it could become a compelling buy for value-minded investors.

HEAVYWEIGHT OUTSIDERS. The Decatur (Ill.) company is well-positioned to take advantage of soaring global demand for basic foodstuffs. As diets improve in developing nations, the market is booming for ADM animal feed and cooking oil. While strong demand will contribute to higher grain and soybean prices—a neg-



BETTER HARVEST COMING: Demand for corn is strong

ative for margins—the asset-rich company can more than compensate by expanding its business and leveraging its status as a low-cost producer.

As for the price-fixing investigation of lysine, as well as citric acid and high-fructose corn syrup, ADM can afford to settle. It carries little debt and a lot of cash. Potential government fines of as much as \$30 million would have little impact. In addition, ADM has agreed to conclude what's considered the most onerous of its civil litigation for \$25 million. The company and once-recalcitrant Chairman and Chief Executive Dwayne O. Andreas are expected to launch talks with federal investigators soon. ADM declined to comment on the probe.

It was clearly the investigation that led to pro-shareholder steps aimed at changing the company from a family-run patriarchy. "We need a board that is

more diversified and more global in approach," says G. Allen Andreas, Dwayne's nephew and a vice-president and counsel to ADM's executive committee. Eight of the 17 directors are expected to step down this fall. Three outside directors have been selected and investors are pushing for more heavyweight outsiders in coming years. As management influence wanes, shareholder moves could follow, such as higher cash dividends and a formal

review between executive pay and stock performance, which are unrelated today.

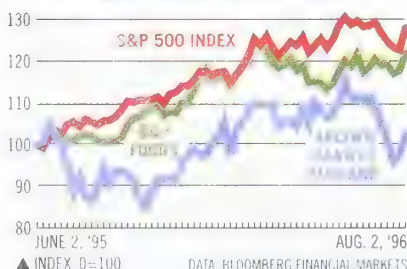
Activists still have plenty of fault. One of the new, elected sweep candidates for the board is a relative of an ADM executive. Such an insular, informal run company may not change stripes soon. "They still don't get it," says Richard H. Kopf, general counsel of the California Public Employees' Retirement System. And investors have reason to worry about succession: Vice-Chairman Michael D. Andreas, son of the 78-year-old CEO, has been told that

and ADM Vice-President Terrance S. V. son will be indicted this fall on charges related to price-fixing. The expected departure of those executives could create a vacuum. "I don't think there's a benefit of people being nurtured as successors," gripes Edward J. Durkin, assistant director of the United Brotherhood of Carpenters' pension fund, which owns 775,000 ADM shares. ADM says more than a dozen company executives are "capable of filling the top jobs."

Still, bullish Wall Street analysts believe that ADM could support a steep price in the mid-20s, vs. 18% on Aug. 7. "The ball has started to roll" in ADM's evolution to a shareholder-driven business, says John M. McMillin of Prudential Securities Inc. The key question is just how fast.

By Greg Burns and Richard Melcher in Chicago

ADM'S STOCK LAGS...



...BUT THE WORST MAY SOON BE OVER

- ADM should cash in on soaring global demand for basic foodstuffs as well as improving outlook for U.S. grain and soybean harvest and easing corn and soybean overcapacity

- Balance sheet is bomb-proof: \$1 billion in free cash and little debt

- Though company can still be arrogant and insular, management is becoming more conciliatory and could settle expected criminal charges

- A sweeping board revamping should create a tighter structure and sensitivity to shareholders

WAST! WANNA LOSE MORE MONEY?

"mini-tenders" being offered for real estate LPs are all too "mini"

Over the past decade, investors in real estate limited partnerships have suffered a kind of financial purgatory. Losses on their investments amount to many billions of dollars. Now, many of these hapless limited partners are being subjected to further indignity: As they attempt to extricate themselves, they are falling prey to the misadventures of real estate firms that are systematically buying up these underwater partnerships at a fraction of their real value. In effect, the limited partners, many of whom are unaware of the real value of their investments, are losing out a second time. And it's all perfectly legal.

Here's how the process works: Real estate firms, most prominently Equity Resources Group, KH Financial (operating under the name Everest), and Macenzie-Patterson, solicit limited partners and offer to buy them out. The firms employ a "mini-tender," which allows them to buy up to 4.9% of the outstanding units, most with a \$100 face value, without registering with the Securities & Exchange Commission—and without disclosing such key details as the LP's market value.

CLUELESS. Many investors are accepting the offers. "It's a quick way to get a unit with no fees or charges," says Eggert Dagbjartsson, executive vice-president of Boston-based Equity sources.

Few of these investors, though, are aware that there is an active secondary market in LP interests. Competition in this market drives prices usually much higher than deals offered by real estate firms to frustrated investors. The firms often pick up interests at discounts of 60% or more (table). Limited partners usually find out later that they sold on the cheap, but then it's too late, because sales are irrevocable. "Limited partners can't have enough information to de-



RAW DEAL

Investment groups are enticing owners of underwater \$1,000 limited partnerships to tender their interests at huge discounts to secondary-market prices

PARTNERSHIP NAME	TENDER PRICE	MARKET PRICE	DISCOUNT TO MARKET
ARVIDA/JMB PARTNERS*	\$100	\$295	66%
CARLYLE REAL ESTATE XI	35	81	57
CIGNA INCOME REALTY I	80	135	41
DAMSON/BIRTCHER REALTY INCOME I	110	220	50
DEAN WITTER REALTY INCOME I	150	321	52
PAINWEBBER EQUITY PARTNERS III	150	251	41

DATA: CHICAGO PARTNERSHIP BOARD, INC.

*TWO REGISTERED TENDERS LATER OFFERED \$420 AND \$435 PER UNIT. THE PRICE WENT AS HIGH AS \$461

termine what the assets are worth so they're clueless that the mini-tender is a lowball price," says James Frith Jr., president of the Chicago Partnership Board, a secondary-market maker.

Firms accumulating these interests expect to realize huge capital-gains profits. Values of real estate LP interests are rising, which is causing more general partners to liquidate partnerships and distribute proceeds to unit holders. In the past two months, more than 90 public LPs have disclosed pending asset sales.

Real estate firms that want more than 4.9% of an LP will employ a regis-

tered tender offer. That can be a better deal for limited partners. Offering documents, for instance, typically disclose secondary-market prices.

Investors solicited through tender offers, especially a mini-tender, should seek out the secondary market. One way is to call the general partner, who will supply names of firms buying partnership units, or act as agents to help sell them. Agents charge commissions as high as 7.5%. Some charge fees of up to \$100 to process the transfer paperwork. Still, Ross T. Bowler, a secondary-market maker in Madison, Wis., says: "The transfer fees and commissions charged in the secondary market don't reduce net proceeds to anywhere near the price offered by the mini-tenders."

One recent deal graphically illustrates the price disparity between mini-tender and secondary-market prices. On June 12, Equity Resources offered to buy 4.9% of ARVIDA/JMB Partners, a troubled land development partnership.

BIDDING WAR. But just a few days later, ARVIDA/JMB got two registered tender offers from Walton Street Capital Acquisition and Raleigh Capital Associates, an affiliate of Leon D. Black's Apollo Real Estate Capital Advisors II. After a spirited bidding war, Raleigh beat out Walton with

a \$435 bid, a big jump from the prevailing secondary-market price of \$295.41 before the price war began. A few weeks later, New York-based Boreas Partners, an affiliate of financier Carl C. Icahn, also made a tender offer at \$460 a unit. Recently, Boreas terminated its offer and joined Raleigh Capital to bid for 46% of the outstanding units at \$461 each. The bidding is now closed, and the tenders are being collected.

The general partner opposed the bid, claiming the units are worth between \$565 and \$610.

Spencer Jefferies, the Dallas publisher of *Partnership Profiles*, a directory of partnerships, says there will probably be more unfortunate limited partners in the future. Mini-tenders are expected to increase for all types of partnerships, he says. Limited partners solicited by mini-tenders would do well to study the ARVIDA/JMB Partners deal. Pity the few limited partners who sold out to Equity Resources before the bidding war began. They cashed out at a miserable \$100.

By Toddi Gutner in New York

By Alison Rea

WHY RISING BANK FEES ARE BACKFIRING

When New York schoolteacher Miriam Faugno was told by her bank 13 years ago that she couldn't see a teller unless she kept at least \$5,000 in her account, she took her business to the bank down the street. But now, that bank's high minimum balances and charges for using automated teller machines have her searching again for a better alternative. "I have the feeling that, in small increments, banks are just sucking us dry," Faugno says.

Faugno is one of a growing number of consumers unhappy with the steadily rising cost of using banks, especially their bewildering plethora of fees on top of low interest rates on savings. And these days, she has plenty of other choices for her banking needs, which include checking and savings accounts, individual retirement accounts, brokerage services, credit cards, and loans. Over the past two decades, numerous mutual funds, brokerages, credit-card issuers, credit unions, and even check cashers have been stealing away customers from banks. These competitors offer comparable products and services at often lower costs. And many pay higher interest rates on customers' balances.

The erosion of banks' market share has been dramatic. From 1975 to 1995, the portion of U.S. household financial assets held in bank deposits fell from 25.8% to 13.7%, according to estimates based on data from the Federal Reserve Board. But that hasn't stopped banks, who are finding it increasingly difficult to make money through traditional lending, from creating new fees and hiking old ones.

LOST LOGIC. Banks say fees not only boost revenues but deter use of expensive products, charge more accurately for services, and chase away unprofitable customers so the banks can focus on selling more to good customers. Unfortunately, most banks aren't very good at executing this strategy. For example, while they are trying to discourage use of expensive tellers and checks, many

banks charge extra for electronic services like computer banking.

Even if some fees make sense, on balance they are almost certainly alienating too many profitable customers. "For years, U.S. banks have gouged consumers with ever-increasing fees.... They are going to scare



**Fee-gouging banks
will lose customers to
brokerage houses,
credit unions, and
mutual funds**

more customers away," says Edmund M. Mierzwinski, a consumer advocate with U.S. Public Interest Research Group. Instead, banks should be wooing people with better service and products. "The point is not to charge customers more but to get more of their business," says David S. Berry, director of research at investment bank Keefe, Bruyette & Woods Inc.

That logic, though, seems lost on most banks. In 1990, the newsletter *Fee Income Report* counted 96 different bank fees. In 1995, it found 290—for everything from unreturned ATM cards on closed accounts to excessive safe-deposit box visits. Most contro-

versially, some banks have started charging noncustomers who use the ATMs a surcharge that usually runs 50¢ to \$1.50 per transaction, but can soar as high as \$10 in casinos and remote locations, according to *Bank Rate Monitor*.

Banks keep jacking up fees, too. In 1990, they charged an average of \$12.54 for a bounced check and \$10.71 to stop payment on a check.

By 1995, this had risen to \$16.73 and \$14.41, respectively, says William Hampel, chief economist at Credit Union National Assn. Now some

banks are even charging a lucrative \$30 per bounced check.

OPTIONS. Banks also are losing business thanks to the niggardly interest rates they pay on minimum balances required to open accounts. Chase Manhattan, the nation's largest bank, pays up to 2.85% on accounts with

\$5,000 in checking and savings

In contrast, Merrill Lynch & Co. pays 4.75% on \$5,000 accounts, and Fidelity Investments pays 4.49% on accounts with \$10,000.

Less affluent consumers have other options, too—thrifts, smaller banks, and especially credit unions, which have lower regulatory costs and pay no income taxes. Fees and minimum balances tend to be lower at all three. Credit unions require an average of \$150 to open a checking account that pays 2.15% interest or a savings account that pays 3.30%.

To be sure, not all banks are rabid imposers of fees, and many are glad to waive charges for their good customers. Some banks have begun omitting fees to attract more business. And a few are skillful at implementing fees to meet strategic goals. But most banks are just driving away people like Faugno.

"They don't need to nickel-and-dime me to death," she says. "They might get less in fees, but they'd have a happy and loyal customer... and if I trusted them, I might buy other things." Hello, banks, are you listening?

Alison Rea covers banking

BY GENE G. MARCIAL

S BERKLEY BEING WOODED?

Even a penny or two in earnings disappointment can send a stock diving. So W.R. Berkley (BKLY) was expected to tumble when the property-and-casualty insurer reported second-quarter operating earnings of 90¢ a share—less than the Street's consensus of 92¢. They didn't: Berkley instead jumped from 41 to 44. Why? Whispers of a takeover.

The insurance industry has seen a string of buyouts this year. The most

AN UPTICK ON BUYOUT TALK



recent was the agreement by General Electric Capital to purchase First Colony Corp. for \$1.8 billion in cash.

"Berkley is being wooed by several larger companies, including giant insurer American International Group (AIG)," says one New York investment manager, who is buying Berkley shares. He notes that Berkley CEO William Berkley and AIG CEO M.R. Greenberg "are close friends and have been talking off and on about a deal." Three years ago, he says, AIG was rumored to have targeted Berkley as a possibility. CEO Berkley says that if an offer were made for Berkley, he would have to consider it because shareholders own the company, and our responsibility is to do what's best for them." But he says AIG hasn't approached him. And an AIG spokesman says there was no truth to the takeover rumor. The money manager who focuses on buyout candidates insists, however, that AIG is very interested in Berkley. He says CEO Berkley recently expressed frustration over the stock's lackluster behavior.

"We believe Berkley will now respond

favorably to a bid of at least 60 a share," says the money manager. Management owns some 15% of the stock. The stock hasn't been much of a performer this year, skidding to 40 in late July, down from more than 50 in early February.

Analyst David Seifer of Donaldson, Lufkin & Jenrette Securities, who is bullish on the company, has a price target of 50, based on an 11.7 multiple on his 1997 estimate of \$4.25 a share and a 1.45 multiple on the book value of 35.

WATCH FOR CNS TO START SNORING

One New York money runner, who manages \$400 million and makes sure he's fully invested in equities, seldom engages in short-selling. When he does, this money pro, who requests anonymity, has to feel that his case is airtight. He's shorting CNS (CNXS), which soared from 3 a share in 1994 to 25 by April, 1996, before easing to 18.

Sales of Breathe Right, which has turned into a near-wonder product, zoomed from \$2.8 million in 1994 to \$48.6 million in 1995. Breathe Right is a nasal strip to reduce, if not eliminate, snoring. Sales have been helped by some football players using the strip, thus attracting kids to the product.

CNS has become "a perfect stock to short," says the investment manager. He feels the first-half results reveal dire prospects ahead: "Earnings were headed in the wrong direction even as sales continued to climb," he explains. In the first half of the year, CNS posted operating earnings of \$6.1 million, or 32¢ a share, down from \$9 million, or 50¢, a year ago. Sales, on the other hand, climbed to nearly \$42 million from \$26.3 million. In the second quarter ended June 30, 1996, operating earnings dropped to 15¢ a share, down from 37¢ a year ago.

"There is a big risk that the company won't hit the 77¢ the Street expects for all of 1996," he warns. When that happens, he says, expect the stock to head south—"down to 9, at best."

Analysts remain bullish, however. For 1997, they project earnings of \$1.07. The money manager, however, expects about 85¢. Breathe Right, cleared by the Food & Drug Administration in 1993, is being sold worldwide by 3M. CNS chairman and CEO Daniel Cohen says second quarter earnings a year ago were helped by lower advertising expenses and tax-

loss carryforwards, so comparisons with this year's second quarter were affected. But he's comfortable with the analysts' estimates for 1996 and 1997. Breathe Right, he adds, has penetrated only 7%-8% of households that could use the product. He sees 1996 sales rising to \$85 million to \$90 million.

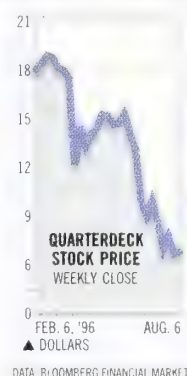
NEW HANDS ON QUARTERDECK?

The floor seems to be collapsing under Quarterdeck (QDEK), a pioneer developer of software for personal computers and the Internet. The stock has been in a downdraft since December, skidding from 39 to 6½ on Aug. 6. Analysts have turned wary about the company since it reported disappointing third-quarter results: a loss of 68¢ a share, vs. a profit of 12¢ a year ago. And revenues dropped to \$16 million from \$28.1 million.

But several California investment managers have been buying: They believe the company, at its current price, has attracted an aggressive suitor, McAfee Associates (MCAF), a maker of antivirus and networking software. McAfee tried to acquire Cheyenne Software in April for \$1 billion. It withdrew its bid for Cheyenne in May after Cheyenne refused to negotiate. Now, McAfee is said to be poised to go after Quarterdeck, whose products for PC and Internet software "fit quite perfectly the direction that McAfee wants to go," says one analyst, who puts the buyout value at 17 a share.

Quarterdeck has been increasing its bet on its Internet-related products, which accounted for more than half of its revenues in the third quarter. The company specializes in providing utility solutions to the Windows market and offers a line of powerful next-generation Internet tools. McAfee Chief Financial Officer Terry Duryea says the company is "considering various types of corporate relationships." But he declined comment on the Quarterdeck rumors. Quarterdeck didn't return calls.

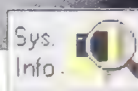
LOSSES HAVE LED TO A DOWNDRAFT



A DESKTOP THAT'S ACTUALLY CAPABLE



*It's not a toy.
But it's pretty
hot in here.*



Talk about considerate. Being
having a thermal sensor that tells you
it's too hot, the new Compaq Desktop
will warn you if its hard drive's about
to fail anywhere. It's all part of what we
call the next generation of Intelligent
Manageability. Among other things.



PENTIUM PRO



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Has It Changed Your Life Yet?

CITIES

BRINGING HOPE BACK TO THE 'HOOD

Does Chicago provide a model for urban renewal?

From behind the rows of dark maple pews at St. Edmunds Church, the Reverend Richard Tolliver regards the cluster of children in prayer. The portly Episcopal priest savors the sight, then turns toward his office, a grin creasing his face. "This is where it all begins," he says. "My vision starts with these children."

When Tolliver took over the pulpit at St. Edmunds in 1989, these pews were nearly empty. Once the place of worship for some of Chicago's wealthiest black citizens, the church had become a towering anachronism amid drug dealers, gangs, and petty criminals. Washington Park, a 12-block patch on the city's South Side, was a sickly urban tract, its once-elegant brick graystones intermixed with decrepit public housing. Some 55% of its population had left by the early 1970s. Of those remaining, 60% lived below the poverty line.

It's not a new story. Middle- and working-class families have fled American cities for decades. With their flight, private-sector investment in urban areas has declined precipitously, hollowing city tax bases and choking off funds for public services and infrastructure. At the same time, a shrinking federal and state safety net has left cities paying more to care for an ever-poorer underclass.

But these days, something remarkable is happening in Washington Park, as it is in small corners of Los Angeles, Cleveland, Boston, and other cities. Mostly through Tolliver's brainchild, St. Edmunds Redevelopment Corp., \$40 million is pouring into the neighborhood, financing construction or renovation of 500 homes within two blocks of the church. Mortgage lending is up 65%. A private school and youth programs are thriving. Dealers and

thugs are moving out, and crime is down at least 15% since 1993.

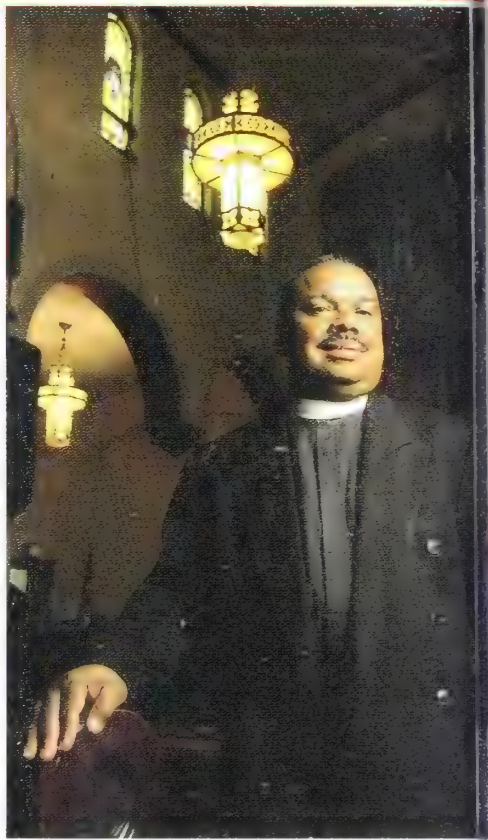
Change is coming from an approach that rejects both big-government, big-money solutions and the 1980s free-market notion that a rising tide lifts all boats. Rather, St. Edmunds is combining public and private money to build homes that, together with better education and lower crime rates, can attract modest-income and working-class families. Tolliver envisions a mixed-income, residential community that attracts a healthy complement of corner stores and restaurants.

The diverse population and solid local economy would feed on itself, attracting yet more residents and business.

Washington Park's strategy represents a radical rethinking of urban renewal, an embracing of private-sector solutions traditionally shunned by the

community-development world. Now, tiny community groups across the nation are partnering with for-profit enterprises, imposing a mutual discipline that forces projects to meet local needs and produce at least modest returns. In Washington, too, Housing & Urban Development Secretary Henry G. Cisneros is racing to shut down failed programs, turning his agency into an incubator of sorts to attract private investors.

Washington Park gives a glimpse of what such partnerships can produce. Other cities are winning comparable results. In Kansas City, Mo., a joint resident-police effort has helped reduce overall crime by 19% in 1995 and another 25% so far this year. Newark's New Community Corp. is majority owner of a Pathmark supermarket that has helped bring shopping back into the city center, low-

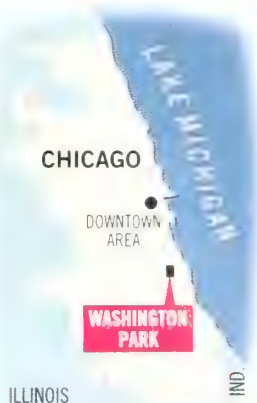


ering food prices; it's plowing its profits back into a broad range of community programs. Just as encouraging is a community-led development initiative in South Bronx, where a stream of new tailors is bringing in jobs.

Undeniably, America's inner cities remain in crisis. Even in Washington Park, poverty has not eased. An undercurrent of resignation, moreover, threatens to undermine early results. Still, the neighborhood is a place of hope. This is the story of one community's attempt to make itself worth living in, representing a modest but workable solution to America's urban crises.

At nightfall, just a few blocks from St. Edmunds, rap music pumps from a boom box into the humid spring air as a group of black teenagers plays basketball on a closed highway ramp. The smell of marijuana fills the air, as onlookers talk rowdily and shake 40-ounce bottles of beer. On other evenings, bloody turf wars have erupted between the Black Disciples, the Mickey Cobras, and other gangs. Stabbings and gunfire are endemic.

But a group of angry residents is taking action. In St. Edmunds' sparsely cement-floored basement, Beverly Catherine, Darryl Starks, and Sydney Simmons have joined nearly 30 other residents to wage war against the thug-





threaten their safety. Instead of sitting on stoops coming, the group finally decided to act, and summoned eight Chicago beat cops to find them.

They play ball 'till five in the evening sometimes," complains a resident. "And I can hear them fighting."

They ain't out there to play," says another. "That basketball court is a camouflage for selling drugs."

The people of Washington Park have lost faith in the ability of a financially strapped city to solve their problems. At the same time, black leaders, locally and nationally, are calling for a new direction as the only true solution. These currents—and a combustible mixture of anger, camaraderie, and pride—are drawing residents here to act. Their roots are in this neighborhood. Why should I let anyone run me out?" asks Beverly Catherine, who has lived in Washington Park since 1956. She and her husband used to bolt their doors as drug dealers from neighboring projects sold their trade on an empty adjacent lot. Two years ago, the couple purchased a 150-square-yard property for \$100,000 and fenced it in. "Now, it's just

'MY VISION STARTS WITH THESE CHILDREN'

Reverend Richard Tolliver of St. Edmunds Church hopes to lure middle- and working-class residents back to Washington Park with the reopened St. Edmunds Academy. Blighted housing is being rebuilt by the St. Edmunds Redevelopment Corp., an alliance of business, activists, and government

officials, but it is Richard Lamar Tolliver who has ignited and focused this self-help movement. "The inner city must be saved block by block," he says, loosening his Roman collar and settling into a sofa in his small office at St. Edmunds.

The 51-year-old Tolliver is hardly the sort you'd expect to find toiling in the 'hood. He is quick to point out his middle-class upbringing in the manufacturing town of Springfield, Ohio. Now, he eschews Washington Park for a home in Hyde Park, a tony enclave a few miles away. He speaks with a professorial air, punctuating sentences with lively arches of his thick brow. He prides himself on his professional accomplishments, including five advanced degrees. Lining his office wall are photographs of him beaming beside Presidents Bill Clinton and Jimmy Carter, Archbishop Desmond F. Tutu, and the Archbishop of Canterbury.

In Chicago, Tolliver is known as among the first to promote the notion that only mixed-income development can stabilize distressed inner-city communities, that their survival depends on recovering the families that abandoned them. They are critical, he says, not



peace and quiet back there," she says.

Starks, 25, believes that only through such individual efforts will things really change. He stands up at the meeting and exhorts: "There's no quick fix. Everything must start small. But we know that we'll never get anything done working from the top down. Change has to start here—from the ground."

The grassroots rumbling is com-



STRUGGLING FOR OPTIMISM

Woody by the area improvements, Sydney and Rene Simmons moved their family to a newly renovated apartment. But they're skeptical of a renaissance. Amanda Carney (bottom) is St. Edmunds' link to money through a large, nonprofit community development group. 'The government can't do everything and shouldn't be expected to,' she says

only because of their incomes and the businesses they draw, but also because jobs and a strong work ethic enhances community life and creates role models for its youth. "You have to attract more than just those who have fallen to the bottom of the social safety net," he says.

On Sundays, Tolliver likes to share his vision with the congregation, many of whom have moved from the area but return for services. He updates them on the housing progress and boasts of school enrollment. Until recently, Tolliver's reports drew little more than blank stares. "They believed in me," he says. "But I'm not sure they believed we could do anything to change this neighborhood."

Now, he can point to results, from the lower crime rate to a new Little League club. Still, Tolliver's strategy is driven largely by the reputation of his church, one of few credible city institutions, and by his own charisma. And even that asset can rub some residents the wrong way. Some dub the pastor an elitist who is distant from the very people he seeks to serve. "I think he only wants to know people who came from his level," says resident Renee Simmons. Adds her husband Sydney: "I don't see him around enough." Says Tolliver: "If you want me to be reinvigorated to take on this task every day, I have to have my space."



the well-intentioned campaigners for Lyndon B. Johnson's War on Poverty. Even her boss says she often fights an inclination to tell poor blacks what's best for them.

Unlike many old-school liberals, though, Carney staunchly believes poor communities must pull themselves out of poverty. "The government, while a critical component, can't do everything and shouldn't be expected to," she says. Carney also believes that in an era of falling government support, cities must be more creative in spending diminished federal dollars. As a consultant for Local Initiatives Support Corp., the nation's largest nonprofit community-development support organization, Carney works at the front lines of reform. She helps Tolliver and St. Edmunds turn private investments into new homes.

Her primary weapon: the Low Income Housing Tax Credit. Enacted as part of the Tax Reform Act of 1986, the measure offers corporate and indi-

vidual investors a credit against their federal income taxes for investments directed at acquiring, rehabbing, or constructing low-income housing. It attracts \$3 billion a year, from companies such as AT&T, Xerox, and BankAmerica, producing about 110,000 low-income rental units. "Do-goodership is not sustainable," says William M. Goodyear, CEO of BankAmerica-Illinois. "Proper business relationships are."

Such investments, funneled through LISC or other syndicators, finance 40% to 50% of development costs; the rest comes from bank loans, grants, and federal aid. Carney, a 1991 graduate of Northwestern University's Kellogg business school, helps Tolliver and his staff administer these diverse funding sources and tries to wean them off money from the government and foundations. She shows them how to deal with banks and how to handle spreadsheets, cash flow, and basic real estate issues.

At times, it has been a struggle. Car-

Amanda Carney, St. Edmunds' link to money, is a product of the affluent, mostly white Chicago suburb of Lake Forest. She strikes some in Washington Park as a 1990s version of

Some housing experts think urban areas can be restored by expanding tax credits and assisting community groups

has clashed with the strong-willed over on everything from staffing decisions to rent levels. He would like to fund St. Edmunds' programs faster, she thinks is prudent. With LISC and her, Carney controls the purse-strings, and she likely will win such decisions. "Asset management is critical to Ed's," Carney says. "It's one thing everyone to come to the ground-keeping, but these units are going on hopefully another 50 years, and they financial controls in place."

through the dim, narrow corridors of St. Edmunds' church, children walk in single file. girls wear blue plaid skirts and white blouses; the boys blue slacks and ties. Their focus straight ahead until they spot the clergyman striding out of his office. "Good morning, Father Tolliver," they out in unison. Tolliver smiles broadly, nods his head, issues a warm "Good morning, children."

beyond all of Washington's new bricks and mortar, St. Edmunds Academy is Tolliver's greatest source of pride. It is so perhaps the most critical element of his vision for redeveloping Washington Park. Of the seven grade schools that are Washington Park, five are among Chicago's worst-performing. Tolliver realizes that to lure middle- and working-class residents, the community must offer families a solid school.

Tolliver spent four years applying to his 600-member congregation for \$400,000 in donations for repairs needed to reopen the 40-year-old academy, which shut down in 1983 for lack of funds. Then he tapped philanthropist Gladys Ray, a retired Chicago public school principal, to run some 42 students attend the academy, which runs from kindergarten through third grade. There's a growing waiting list, and enrollment is expected to rise each year as the school adds successive grade levels through junior high.

The problem: St. Edmunds still isn't drawing many middle-class students from other neighborhoods, so most students come from Washington Park. Their parents can't afford the \$3,000-per-year tuition, so the school has constant

fundraisers. Still, Ray says, "It is important that this be a mixed-income school."

Two weeks after the meeting with police, Sydney Simmons stands on his rear balcony, looking down at a trash-strewn lot below. Dozens of children are laughing and playing. Simmons says he'd like to let his kids join the frolic, but the makeshift playpen is too littered with rusted cans, bottles, and muddy pools of insect-laden water to let five-year-old Alexandria and one-year-old Sydney Jr. play there. "If I

will enter first grade this fall. Still, Simmons admits to doubts about Tolliver's grand vision of an urban renaissance. In fact, he sometimes wonders whether the priest and Chicago's police are window-dressing deep, intractable problems that ultimately require government.

Tolliver shares the frustration. "We're on the verge of something great, but it won't happen overnight," he says. He recognizes, too, that some government involvement is both inevitable and desirable. Washington Park's rejuvenation can have only a limited effect without a broader strategic plan to revitalize surrounding neighborhoods and commercial districts—and, arguably, the city as a whole.

As it stands, Tolliver is pleased with St. Edmunds' progress. True, its balance sheet is highly leveraged, and cash flow is squeezed by five undeveloped buildings it is carrying; Tolliver has relied on LISC for a \$400,000 loan to help cover costs associated with new projects. But the promise is clear. If St. Edmunds can raise enough to renovate its empty buildings, it will generate a steady stream of management fees to put into new projects. "St. Edmunds is on an unbelievable growth curve," Carney says.

Is Washington Park replicable on a broad scale? Some critics think not, since such community-based programs necessarily derive success from their small, tightly focused structures. The movement also doesn't solve the problems of low wages and joblessness that plague inner cities. "They have not done all that well

in terms of economic development," says Margaret Weir, a senior fellow at the Brookings Institution.

Think of the power, though, of a thousand Washington Parks and a thousand Richard Tollivers, each renewing a neighborhood block by block. It is a model that resonates, as the federal government, more than ever, is relinquishing its role as the check writer for cities. Indeed, some experts think that the way to restore American urban neighborhoods is to expand the Low Income Tax Credit and provide grants for technical assistance to the local groups that would best deploy the resulting investments. Block by block, cities could become places people want to live in once more.

By Ron Stodghill II in Chicago

GRASSROOTS GROWTH

Across the country, local groups are working with private-sector investors to spur development:

LOS ANGELES A Community of Friends has renovated more than 300 apartments, most for handicapped low-income residents, helping to restore blighted sections of Boyle Heights.

MIAMI Tacolcy Economic Development Corp. has helped rebuild Edison Plaza, a shopping center damaged by the 1980 riots. The renovation, including a new supermarket, created 150 jobs.

NEWARK New Community Corp. has built over 2,500 apartments in two decades, plus seven day-care centers, a supermarket, and a nursing home.

NEW YORK CITY Harlem's Abyssinian Development Corp. has developed 375 housing units for low- and moderate-income residents and has launched several commercial projects.

SAN ANTONIO Project Quest, formed by local churches to train and place laid-off garment and military workers, has put 600 residents in new jobs.

DATA: COMMITTEE FOR ECONOMIC DEVELOPMENT, BUSINESS WEEK

had my way," Simmons says, "I'd move out to the suburbs."

If Washington Park is enjoying a new sense of self-sufficiency and hope, it also is struggling to maintain optimism. The Simmons moved to Washington Park a year ago. Combining his own income as an animal caretaker at University of Chicago Hospital with his wife's part-time earnings, they jumped from a \$475-per-month two-bedroom flat to a renovated, \$670-per-month four-bedroom apartment owned by St. Edmunds.

It's a financial squeeze, but worth it, Simmons says. Clean and sparsely furnished, the new home has enough space for Sydney Jr. to have his own bedroom. It also is just a block from St. Edmunds Academy, where Alexandria

AIRLINES

NORTHWEST: THE TURNAROUND BILL ARRIVES

An ESOP saved the airline. Now labor wants its due

Northwest Airlines CEO John H. Dasburg has been flying high for the past three years. The carrier has posted record profits, paid down billions in debt, and repaired badly damaged relations with its unions. A strong economy and travel-happy consumers certainly helped. But underpinning the turnaround was a three-year employee stock ownership plan that staved off bankruptcy in 1993 by giving employees a 30% equity stake in exchange for

halted," predicts Michael Lowry, publisher of *AirWatch Report*, a newsletter in Oswego, Ore.

Dasburg's biggest challenge is to establish a new relationship with labor. Northwest's 45,000 employees don't see themselves as worker-owners the way those at majority-owned United Airlines Inc. do. Instead, they view the ESOP as an emergency loan to keep the company afloat. Indeed, the unions have said flatly they don't want to renew

the Northwest local of the International Association of Machinists.

Dasburg will have a difficult time pleading poverty. In late July, Northwest posted a 94% increase in second quarter profits, to \$203 million. And in 1994, the company earned a record \$1.1 billion. Dasburg concedes that the turnaround is likely to "temporarily damage" management's relationship with employees. That's because he's determined to keep expenses in line with those of rivals. "We will not allow our costs to rival those of Richard B. Hirst, Northwest's senior vice-president for corporate affairs and top negotiator."

This kind of talk has union leaders edgy. They're not sure how many productivity improvements are still available. Even before talks begin, there are signs that labor and management aren't on the same page. Under the 1993 ESOP contract, pilots get up to a 3% raise on top of their snapback, based



DC-9 OVERHAUL: \$886 million in concessions. Mechanics put in extra hours without overtime pay

Now the ESOP is drawing to a close, and Dasburg suddenly is heading into chop. Wages at Northwest Airlines Inc. will "snap back" by 12%, to 1993 levels, while rivals hold theirs steady or reduce them. The added cost will crimp cash flow, constraining Northwest's ability to modernize its aging fleet and pay down the remaining \$2.7 billion in debt (table).

OPTIMISTIC. Northwest's harmonious labor relations may be endangered as well. Management is determined to offset any pay hikes with work-rule changes that lift productivity. Yet union leaders want raises on top of the snapbacks already due. Dasburg is optimistic that the problems can be overcome. But management and labor already have begun to clash. "The strong improvement over the past few years will probably be

the ESOP by taking more pay cuts.

Nor has Dasburg built a culture of worker participation. Aside from a successful employee suggestion program, there are no task teams to reengineer work or efforts to bring workers into decision-making. That's in contrast to United, which has teams tackling everything from cash management to fuel use. While today's cooperative labor relations won't unravel immediately, "the worry is what happens two or three years down the road, when all this employee ownership is forgotten," says Corey Rosen, head of the National Center for Employee Ownership in Oakland, Calif.

The battle over pay is just heating up. The 12% snapbacks began to go into effect on Aug. 1. Because the raises only restore them to 1993 levels, union leaders want added pay hikes in the new contracts. "We've lived through the downside. We also want in on the upside," says Marv Sandrin, president of

CRUNCH TIME AT NORTHWEST

How the end of a 1993 employee stock ownership plan will hurt

RAISE LABOR COSTS Wage snapbacks of 12% will add \$280 million to the company's \$2.4 billion payroll

SLOW DEBT REPAYMENT Aggressive debt reduction, which lowered the level from \$4.5 billion in 1994 to \$2.7 billion today, will be hard to sustain

STALL NEW PLANE PURCHASES Northwest, whose fleet already is 19 years old vs. 11.6 for rivals, will have less money to buy new aircraft

DATA: NORTHWEST AIRLINES INC., BUSINESS WEEK

on a formula tied to average pay hike at rival airlines. But when Northwest pilots said recently that they expect an extra 3%, Northwest said it wanted the issue arbitrated. "We were dumbfounded," says Paul Omodt, a spokesman for the Air Line Pilots Assn. "It's fairly simple math." Dasburg attributes the dispute to ambiguity in the formula.

Still, there are some signs of cooperation. Management has agreed to keep labor's three board seats for 10 more years, even though the ESOP's equity stake will dwindle as employees retire and cash out. And recently, mechanics at Northwest's maintenance base in Portland agreed to work four 10-hour days a week without overtime pay to clear up a backlog of DC-9s that require heavy maintenance. That kind of teamwork helped give Northwest three fat years. The trick will be to keep this soaring airline from losing altitude.

By Susan Chandler in Chicago

THE WHITE HOUSE S. THE GREENHOUSE

ersing course, the Clintonites get behind emission controls

ist month's call by the U.S. for
mandatory limits on pollu-
ants that can lead to
al warming has sent
s waves through the
rican energy indus-
As the world's
st producer of
ghouse gases, the
had long op-
d mandatory re-
ons. On July 17,
ver, Timothy E.
h, the Under
etary of State for
al Affairs, sur-
ed industry ob-
ers and environ-
alists with a
atic reversal at a U.N.
ate change meeting in
va.

ie administration's embrace of
latory limits is seen as more than
cal posturing: It has set the stage
nore serious negotiations. In 1992
e Earth Summit in Rio de Janeiro,
tiators called only for voluntary re-
ons in emissions to 1990 levels by
That effort to reduce greenhouse
emissions has fallen far short.
January, the U. N.'s Intergovern-
al Panel on Climate Change (IPCC)
the "balance of evidence" suggests
e is a "discernible human influence
lobal climate." It was the first time
the panel, made up of scientists
around the world, had said that
effects of greenhouse gas emissions
e being felt.

DS, STORMS. The IPCC predicted
the atmosphere would warm 2 de-
s Celsius by 2100. That doesn't
d like much, but it could lead to a
ety of unpredictable climate
ges that could spawn more floods
storms and disrupt agriculture
nd the world.

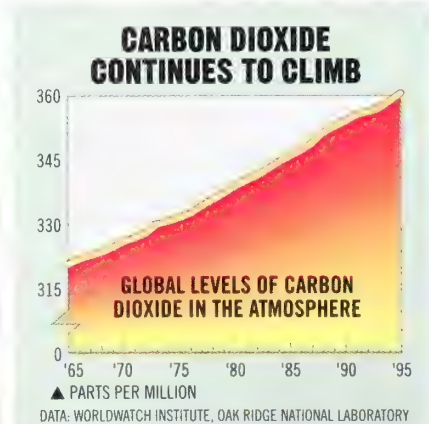
researchers continue to debate the
equences of global warming, but
e is no debate over the rise in at-
pheric carbon dioxide—one of the
important greenhouse gases. Car-
dioxide levels have climbed sharply



in recent years (chart). By some esti-
mates, global carbon dioxide emissions—
mainly produced by the burning of coal
and oil—may increase 60% in the next
two decades, with most of the growth in
China and the developing world.

Unsurprisingly, the energy industry
is fighting mad. John Shlaes—the ex-
ecutive director of the Global Climate
Coalition, which represents coal and oil
interests—calls mandatory emission
caps “an energy-rationing program for
Americans.” Shlaes had expected the
Administration to stop short of manda-
tory limits.

Rio's nonbinding agreement has al-



ready had an impact—thanks mainly
to efforts by the utility industry. Ac-
cording to Michael Oppenheimer, se-
nior scientist with the Environmental
Defense Fund, U.S. emissions would
have grown 13% from 1992 to 2000 in
the absence of the Rio accord. Instead,
says Oppenheimer, they will probably
grow by 7%. He sees that as a sign
that steeper reductions are possible.
“Even in a period of moderate eco-
nomic growth, without a binding agree-
ment, we reduced the expected growth

of greenhouse gases by one-half,”
he says. Mandatory limits would
accelerate that decline, he says.

Companies that invest in
conservation and alternative en-
ergy support Wirth's proposal—
as long as it offers flexibility. For
example, businesses advocate
swaps that would allow them
to build a clean-coal plant in China,
say, and earn emis-
sions credits
back home.

Says Michael L.
Marvin, executive di-
rector of the Business
Council for Sustainable
Energy, a group that
represents energy-effi-
cient companies: “I

think we want to make sure that main-
taining a healthy economy is as important
as any other goal” in the negotiations.

SQUISHY PREDICTIONS. Although the
U.S. called for mandatory limits, it did
not say where those limits should be
set. U.S. negotiators said only that
they support a specific, attainable tar-
get by 2010 or 2020, according to
Eileen B. Claussen, the Assistant Sec-
retary of State for Oceans, Environ-
ment, and Science. A final agreement is
due by December, 1997.

One problem is that no one knows
exactly what the economic impact of
mandatory limits will be. Computer
models intended to project possible con-
sequences make notoriously squishy
predictions. “Any answer can be ar-
rived at through small manipulations
of initial assumptions,” says Hadi
Dowlatabadi, a global change expert at
Carnegie Mellon University.

Despite the economic uncertainty,
there are already encouraging signs of
a consensus. At the end of the Geneva
meeting, all but 14 countries had ten-
tatively endorsed the U.S. proposal.
Holdouts included the 11 OPEC nations
and Russia. Many clearly see the U.S.
proposal as an important step in a long
negotiating process.

By Naomi Freundlich in New York

COMPUTERS

PLUG AND PLAY? IN YOUR DREAMS

But the PC industry is determined to change that

At first, Sam Kimball was thrilled with the \$4,000 Micron Technology Pentium PC he bought recently. The head of a Manhattan music-production company, Kimball hooked up a modem, tape backup drive, color scanner, and his two-year-old Hewlett-Packard color printer through a port on the scanner. The old printer went on the fritz, so Kimball shelled out \$400 for a newer HP model.

That's when Kimball's nightmare started. The port that had worked fine before was incompatible with the new printer. He spent an extra \$100 for a special cable and circuit card. Then came hours of wrestling with a variety of hardware "interrupt" conflicts—messages in computerese that indicate, for example, that the mouse is on the same setting as the scanner. Finally, he found another card that fit the bill. "I'm going through an experience that is driving me bananas, and I can't imagine what the less high-tech-oriented [consumer] would be doing at this point," he says.

Where do you want to go today? Notwithstanding Microsoft Corp.'s ad line—or which brand you buy—the truth is, it doesn't much matter: You'll end up in PC hell. Despite two decades of fast-paced technological development, the industry has yet to come up with a product that can truly be called simple to use. Last year's arrival of Microsoft's Windows 95 operating system—which brought the PC closer to Apple's Macintosh, long heralded as the ease-of-use champ—fell short of the mark. "These things are like untamed beasts, and we use them because we have no choice," says Paul Saffo, a director of the Institute for the Future.

Ease of use wasn't that high a priority so long as office machines dominated the industry. For the most part, computer companies in those days dealt with a gearhead who purchased all the tech equipment for a corporation, not ordinary consumers who want PCs to work like TVs. But with corporate demand slowing, PC makers realize their

growth depends on reaching the nearly two-thirds of U.S. households that don't own a computer. Moreover, with new, consumer-savvy competitors such as Sony entering the market, PC executives revving up for the next holiday season finally have made simplicity a top priority. "People are only going to buy new computers if they're going to get better and easier to use," acknowledges Mal D. Ransom, Packard Bell NEC Inc.'s vice-president for marketing.

ERROR MESSAGE. How does the industry get from here to there? For a start, the newest PCs incorporate such conveniences as one-button access to online services. And manufacturers are starting to use the Internet to cut the workload of help desks by sniffing out potential problems or delivering the latest software. IBM is planning a World Wide Web site customers can tap into to determine whether they need a software update. If they do, the software will be downloaded automatically.

Meanwhile, PC and software companies, led by Microsoft, are devising a standard called the Simply Interactive PC, or SIPC, which they say will make next-generation machines more like consumer appliances. Microsoft hopes the effort will lead to friendlier devices that can help PC makers crack the mass market. The initiatives, which will be phased in during the next two to three years, include a concept called On Now: PCs that power up as quickly as a TV.

But the industry has a long way to

go. "This technology is not as easy as needs to be," says James A. Firestone, general manager of IBM's consumer division. For one thing, PC makers just resist jargon. Consider this puzzling sage on a Windows 95 PC running Alca Online: "Manager: Error: Independent within independent. Ignoring Errors still abound—indeed, not of the vaunted Macs are immune. P. Trilling, a Manhattan video director, bought an Apple PowerBook that inexplicably turning on when he fo down its lid. It was exchanged for unit that couldn't read any floppy disk."

The industry has largely ignored consumers such as Trilling. After the prices drop their \$2,000 to \$4,000 on a they far too often find themselves spurned by manufacturers and resellers alike. Need help figuring out a complex software program? Be prepared to pay. Microsoft, for one, charges \$1



**THE WAY
OUT OF
PC HELL?**

PROBLEM

The computer is too darn complicated to learn and difficult to use.

SOLUTION

Companies are paying more attention to design. PCs from Packard Bell Compaq have shortcut buttons for features as E-mail and the Internet. Compaq's new Presarios have a button that takes users directly to a help screen where they can learn certain tasks or connect to a live tech rep.

per incident after 90 days for soft-support. And it's a good bet you have trouble getting through. When ad a problem with his new PC, is Klein, owner of a Long Island, cleaning business, couldn't reach a voice at Gateway 2000 Inc.'s tech-support center, even at 4 a.m. That kind of disregard for the cus-r is finally starting to change. ked by return rates as high as 20%, executives have been pumping lots of y into better customer support. quest Inc., a market-research firm n Jose, Calif., estimates that tech-ort centers will receive some 200 m calls in 1996, costing companies llion. Since 1989, the ratio of sup-staff to total employees has gone 1 in 12 to 1 in 6.

KING IN. Better support isn't the answer. Hardware vendors, such M and Compaq Computer Corp., considering direct-marketing ap-es in which company representa-could periodically check in with

PC owners after a sale. An IBM rep, armed with historic data from the help desk, might call or E-mail customers at the six-month mark to provide answers to frequently asked questions.

Manufacturers also are paying more attention to design. New PCs from Compaq and Packard Bell have buttons that provide shortcuts to the phone-answering device, audio CD, and other features that used to require maneuvering through layers of software. Big Blue is working on a model for customers who want to use their systems without straining their backs reaching under the desk to load software onto a minitower. IBM has taken the CD-ROM, power button, and floppy drive out of the tower and put it in a slim package under the monitor.

Even chip giant Intel Corp. wants to make personal computing a snap. The company is pushing an initiative called the Universal Serial Bus, or USB, a speedy pathway it claims will enable users to connect any number of peripherals with the same plug. Another stan-

800,000 queries a week in the service portion of its Web site, where consumers post questions, download software, and read technical articles. Hardware vendors are considering giving customers a free year of Internet access, along with one-button access to sites that might provide service and support. **WIZARDRY.** For over a year now, such companies as IBM, HP, and Packard Bell have been able to tap into a customer's computer remotely, via modem. But tomorrow's computers may be smart enough to detect problems before they happen, automatically notifying the consumer, say, when the hard drive is about to crash. Compaq employs such technology with its network servers and plans to add the feature to consumer PCs in a year or two.

SystemSoft Corp. in Natick, Mass., plans to help PC makers cut down on technical support calls by 25% to 30%. The company will license "call avoidance" products that hardware makers will build into PCs to identify and re-

solve common problems. For example, when an application crashes, SystemWizard will automatically jump into action. If the sound isn't working, users can click on a picture of the speakers, then respond to questions to pinpoint the difficulty. If

the machine can't fix itself, it would dial up a tech-support server or even call a live representative. AST Research Inc. and Digital Equipment Corp. have signed on so far.

If consumers have to call a technical help desk, the idea is to get them off the phone, pronto. Seattle-based Primus Communications is working on a remedy that would allow support engineers to gather solutions to technical problems as they happen and store them in a database. Since the same types of calls keep popping up, a quicker diagnosis will theoretically lead to less time on hold.

Such efforts by computer manufacturers are only a start. But it may at least be enough to help consumers out of PC hell and into limbo.

By Edward C. Baig in New York, with bureau reports

With return rates running as high as 20%, the industry is pumping money into better technical support and self-diagnostic software



dard, known as the IEEE 1394 serial bus or FireWire (an Apple trademark), aims to do much the same thing. The standards are meant to abolish the incompatibilities that haunt so-called Wintel PCs—those built around Intel chips and Windows software. Because no one company controls the design, Wintel PCs have evolved in a Balkanized manner, wherein anyone can come up with a product that may or may not work with any other.

Eventually, the Internet may emerge as the best tool for frustrated consumers, though at present figuring out where to go—and getting there quickly—can be a major hassle. An increasing number of companies are using the Web to cut down on support calls and improve response time, though this solution works well only for Net-savvy customers. Still, Microsoft fields about

SOLUTION

The World Wide Web. Folks can visit sites, such as Tuneup.com, for routine PC maintenance (scanning for viruses, updating drivers). Tomorrow's computers may be smart enough to detect problems before they happen, automatically notifying users when a hard drive, say, is about to crash.

PROBLEM

My machine is seemingly out of date the moment I take it out of the box.

SOLUTION

This is a tough one. But a Microsoft-led initiative called the Simply Interactive PC promises to make it easier for users to upgrade by popping in a larger hard drive, multimedia peripherals, and other devices without opening the machine.

SEMICONDUCTORS

GaAs GUZZLERS ON THE INFO HIGHWAY?

Demand for superfast gallium arsenide chips is soaring

A handful of chipmakers are striking it rich by giving many new electronics products the "gas." That's the chip industry's nickname for gallium arsenide (chemical notation: GaAs), a semiconductor material inherently much faster than silicon.

Long considered a technology in search of a home, gallium arsenide always seemed to just miss out. At first, "gas" found eager customers among military and aerospace companies, which were willing to pay double—or even much more—to bypass silicon's speed limits in microwave communications and radars. Then the cold war ended. Then, supercomputer companies figured that GaAs chips could juice up their next-generation computers. But Intel Corp. trimmed the prices of silicon microprocessors so much that it was cheaper to boost speed with multiple silicon chips instead.

Finally, GaAs is finding its niche—in civilian communications. As a result, the gallium-arsenide business is bucking the slowdown in the semiconductor industry. No signs of a slump here. The top three U.S. producers—Anadigics, TriQuint, and Vitesse—have posted recent quarterly sales increases of 27% to 57% over the same periods last year. Crows Joseph I. Martin, a vice-president at TriQuint Semiconductor Inc. in Beaverton, Ore.: "The phoenix is rising again."

Gallium arsenide's resurgence stems from an ever-expanding profusion of applications. For example, L. M. Ericsson's latest cellular phones have gallium ar-

senide chips to boost performance. Scientific Atlanta Inc., a leading producer of cable-TV gear, recently unveiled equipment that harnesses GaAs to add 50 channels of new capacity. And direct-broadcast satellite receivers need the extra speed to decode digital TV signals.

Gallium arsenide's speed might even be the key to digital TV that doesn't give headaches to people like David M. Fellows, a senior vice-president at Continental Cablevision Inc. He has a rare "golden eye" that makes him ultrasensitive to the defects in digital-video broadcasts.

"If it's a good picture, I just get a headache," he says. "If it's bad, it makes me sick."

PRESSURE. Demand for GaAs is projected to soar still higher as telecom companies launch new wireless services. Some analysts even worry about short-term chip shortages. "The market for GaAs, beginning next year, should start growing at 50% to 60% a year," says Drew D. Peck, technology analyst at brokerage Cowen & Co. That could put pressure on chipmaking capacity.

GaAs chipmakers are not about to let this opportunity slip through their fingers. TriQuint broke ground for a new chip factory in Hillsboro, Ore., July 1. A few days later, Vitesse Semiconductor Corp., based in Camarillo, Calif., announced it will use the proceeds of a recent public offering to build a \$75 million GaAs facility. And at the end of July, Anadigics Inc. in Warren, N.J., said it would spend \$35 million to double its GaAs capacity.

Only \$75 million or less for a new chip-making factory? Yes, because gallium

arsenide plants are much smaller than billion-dollar semiconductor plants that crank out silicon chips. Sales of GaAs chips also are in comparison. In 1994, semiconductor sales climbed to \$10 billion, the industry says, but GaAs sales on the open market were less than a half of 1% of total, \$590 million. Mainstream chipmakers can't be bothered with such a squeak, although gallium arsenide demand this year should jump 24%, to \$730 million worldwide (page 10). Tack on internal production by such electronics giants as

Motorola Inc. and Fujitsu Ltd., and this year's GaAs market could top \$1 billion for the first time.

The advantage that GaAs has always enjoyed is speed: Electrons zip through its silver-gray crystal at least five times faster than they move through silicon. Until recently, that speed came at a high price. The wafers on which GaAs chips are printed were so tricky to process they once cost more than 10 times as much as silicon. And in chip plants, the wafers were difficult to process, driv-



SENSITIVE EYES

David Fellows' rare condition—digitized TV sickens him—might be solved by GaAs chips

GaAs Chips Find a Home

Digital traffic is jamming up. GaAs chips operate at higher frequencies to boost capacity for TVs and wireless phones.

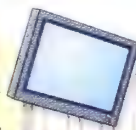


750 Mhz

Today's cable TV
110 channels

1000 Mhz

Tomorrow's cable TV
160 channels



900 Mhz
Conventional cellular phones

Peak performance range for silicon



1900 Mhz

Next-generation wireless phones

hip costs even higher. Recently, s have been falling as both wafer ers and chip producers perfect man-uring techniques. Many GaAs chips arry premiums of 30% or more. But new products are designed from ery outset with an eye to exploiting features, says Anadigics President ld Rosenzweig, "the final solution e even cheaper than silicon."

atever the price, GaAs makers are g customers who are willing—or elled—to pay the piper. To handle urge in traffic in wireless phones, hone frequencies are being jacked from 900 megahertz to 1.9 ertz in tomorrow's so-called person-ommunication services (PCS). At those encies, GaAs is essentially the only . Already, all new cell phones sold U.S. by Ericsson, the third-largest ier after Motorola and Nokia, use igics chips, says Nils Rydbeck, vice-ent of Ericsson North America. "It d a year ago, and we're now using on a large scale overseas as well."

ER LIFE. Higher speed isn't the eason. Gallium arsenide also has a r signal-to-noise ratio. That means hones can wander farther from their base stations. And GaAs chips can sume far less power, so wire-less models can either get by with smaller batteries or offer longer bat-tery life.

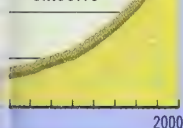
Then comes iired telecom business. As the use one lines has exploded with fax missions, modem data, and local-network traffic, phone companies aving a tough time keeping up. "If an help them move 16 times the down the same fiber-optic cable, i makes economic sense," says se President Louis R. Tomasetta. r only alternative is burying more "

ble-TV systems will come under the hen cable modems turn the con-m to the TV into a lane of the In-tion Highway. Videoconferencing out still more pressure on phone and cables. Utility companies are ng to transmit meter readings from s to central receivers. And by e's end, GaAs will help keep auto e flowing, thanks to collision-avoid-radars in cars. All in all, it looks like ech products will be "cooking with " for years to come.

Larry Armstrong in Camarillo, , with Otis Port in New York and n V. Brull in Tokyo

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They're The McLaughlin Group. Each with a view that's contentious and contagious. (clockwise from left) Jack Germond, Clarence Page, John McLaughlin, Eleanor Clift, Morton Kondracke and Fred Barnes.

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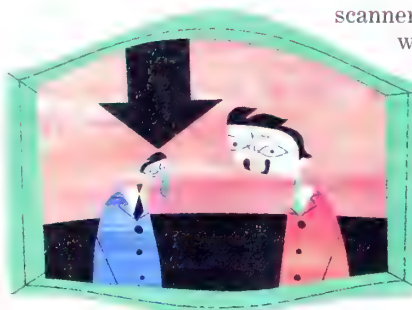
Developments to Watch

EDITED BY NEIL GROSS

STRAIN ON THE BRAIN

CONSTANT STRESS MAY BE MORE THAN just nerve-racking. It may kill nerve cells outright, causing a key part of the brain to shrink. Recent studies in rats show that sustained exposure to stress-induced hormones produces permanent damage in the hippocampus, a seahorse-shaped brain structure involved in learning and memory. Now, scientists are finding similar effects in people.

At Washington University in St. Louis, Yvette I. Sheline, an assistant professor of psychiatry, knew that stress hormones such as cortisol are produced during bouts of depression. She wondered whether high levels of the hormones left their stamp on the brain. Using a high-resolution magnetic-resonance



scanner, she compared women who had a history of depression with others who did not. She found that the hippocampus was, on average, 12% smaller in women with multiple episodes of depression. Other researchers have discovered similar, small hippocampi in Vietnam vets and child-abuse victims with post-traumatic stress disorder. Sheline admits the smaller hippocampi may be the cause, not the result, of these disorders. But given the animal experiments and new human studies, stress hormones look like bad news for the brain.

John Carey

COMPUTER, MAKE ME A... CONVERTIBLE

YOU CAN'T ACCUSE JAMES C. Fischbach of short-term thinking. He's spearheading a 50-year effort called Initiative 2050 to devise a Star Trek-like machine called a

mers. The idea is to project a 3-D, computer-generated hologram of the desired object into the vat. Polymers exposed to the hologram's focused light would

solidify; the rest would remain liquid. Within seconds, a completed object could be pulled from the soup.

The concept leapfrogs an existing technique called stereolithography, which

builds solid objects with a laser beam that sweeps back and forth through a mass of light-sensitive polymers. In-

stead of this bit-by-bit approach, holograms could engender objects all at once, says Fischbach, principal investigator at American Propylaea Corp. in Birmingham, Mich. And special-purpose polymers could yield materials with a variety of properties such as superhard, transparent, and magnetic.

Armed with a \$500,000 grant from the U.S. Air Force, American Propylaea has already developed full-color, 3-D images that hover in space. That has attracted the attention of Big Three auto makers. Chrysler, for example, might use holography to speed up auto design, says Michael C. Holmes, a Chrysler computer-systems manager.

Peter Coy



HOLO-MOBILE: A 'vette from a vat?

"durable product generator" that would create objects of any kind, on command, from a vat of light-sensitive poly-

INNOVATIONS

■ While Americans huddled around conventional TV sets to watch the Olympics, millions of Japanese saw the games on wide-screen TVs—a popular spin-off of Japan's three-decade high-definition TV effort. Designed to mimic movie screens' wider view, these displays may soon mi-

grate to personal computers. Sharp Corp., the world leader in liquid-crystal displays, is preparing a desktop PC with a wide LCD that would be well-suited to viewing spreadsheets as well as digitized film clips. Another advantage: Long rectangular notebook PCs would fit better on the tray tables of an airplane seat.

■ A report from the Aaron

Diamond AIDS Research Center in New York suggests that some people may be protected from HIV infection, even if they are repeatedly exposed. The key seems to be a defective version of a gene for a T-cell receptor. People with the mutated gene don't make so-called CKR-5 proteins that stick out of T cells and act as a gateway for HIV.

A BETTER BREAST SCAN?

WOMEN GENETICALLY disposed to getting breast cancer and those with fibrocystic disease often undergo frequent X-ray screenings. Unfortunately, there is a high ratio of false positive readings, which typically lead to needle biopsy. That procedure is expensive and can be traumatic.

Research by Eva M. Sevick-Muraca, associate professor of chemical engineering at Purdue University, suggests there may be a better way. She and her colleagues have applied for a patent on a method for exposing tissue to harmless, near-infrared light from low-power laser diodes. The light would excite tissue molecules, which would then relax back to a ground energy state, releasing fluorescent light. Researchers could analyze the light values using computer programs developed at Purdue to extract biochemical data, such as the oxygen level and acidity of the target tissue. This information, in turn, would provide a window on early-stage tumor development, which is usually missed by mammography and other imaging technologies.

An added benefit: The equipment would be far less expensive than either X-ray or MRI gear. Sevick-Muraca's lab has developed detailed computer models of how such screening would work. The scientists hope to begin large-scale animal trials this year.

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwaug@businessweek.com

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EDITED BY AMY DUNKIN

GOING FOR THE GREEN IN THE PINK SHEETS

Tired of paying ridiculously high multiples for a stake in hot growth companies only to see their share prices get clobbered? There are alternatives. While the NASDAQ market was taking a recent beating—down almost 20% from its high

in May—another section of the over-the-counter market was quietly chugging along, seemingly immune from earnings disappointments and fickle investors.

Hidden among the shadows of celebrated NASDAQ superstars such as Microsoft is a less well-known part of the OTC market, the “pink sheets.” They’re a compilation of the bid and ask prices of some 20,000 stocks, most of which aren’t listed on any exchange. Often associated with bankrupt firms and penny-stock scams, the pink sheets are also home to some 300 bona fide moneymakers that have been trading at discounts to their book value in relative anonymity. Many are household names such as mapmaker Rand McNally and Houlihan’s Restaurant Group.

ILLIQUIDITY. These companies are all but ignored by the professional investment community, and many outfits want to keep it that way. Although most have had a public offering, families and officers control much of the stock, so they’re not eager for new shareholders. A dearth of in-

formation and lack of liquidity are why many of the stocks are undervalued, says Binkley Shorts, senior vice-president at Wellington Management in Boston.

Until recently, learning anything relevant about these

closely held, thinly traded companies has

been next to impossible. “These aren’t companies you can just ask your average broker to investigate for you,” says Edward McLaughlin, a professional investor in Vero Beach, Fla.

Now, however, a reference book is available that sifts through the junk that litters the pink sheets. It offers in-

formation on the OTC bulletin board, a real-time quotation service for 5,500 companies. “None of these companies is under any obligation to report to the Securities & Exchange Commission (SEC). But if they don’t, they can’t list on any of the major exchanges,” says Peter Salmon, the NASDAQ’s assistant director for trading and market services. In addition to per-share data—such as price-earnings ratios, book value, and dividends—the guide lists the market maker for each issue and tells whether a regular stockbroker or pink-sheet specialist is required. More than half of the companies in the book

don’t report to the SEC, so you won’t find their financials in databases such as the SEC’s EDGAR.

While publisher Harry Eisenberg, a CPA in Lafayette, Calif., has done the legwork, even becoming, in some cases, a shareholder in the nonreporting companies to gain access to their data, he cautions readers that the book is only a starting point. It’s a secondary source, so you’ll need original financial statements and reports to make sure the data is up to date. Many of these companies look good on paper, but because

they’re insular and secretive, they can be prone to malfeasance or reversals of fortune. “You have to take a hobby approach to investing in this area,” says Jack Norberg, a pink-sheet specialist and pres-

INVESTING

Buying Tips

STICK WITH INDUSTRIES YOU KNOW

Check business journals, trade publications, or the NASD’s *OTC Bulletin Board Company Directory* (301 590-6578, \$12) for information or news on the company

ASSESS THE COMPANY’S VALUE

Walker’s Manual of Unlisted Stocks includes indexes ranking companies by p-e ratio, earnings growth, etc.

CHECK FOR SEC FILINGS If the company files reports, you can request proxy statements, 10Ks, and other data

CALL THE COMPANY If a company is shareholder-friendly, it will send you documents. If not, you may want to buy one share of stock to gain access

GET A GOOD BROKER Call the market-maker that *Walker’s* cites for the stock and ask for a broker recommendation

vestors a window into this oft-murky market. *Walker’s Manual of Unlisted Stocks* (800 932-2922, \$75) contains four years’ worth of financial details on 500 companies that list their stock in either the

ident of Standard Invest in Tustin, Calif. “This is for the passive person.”

Indeed, the traditional investment rule applies: Buy only what you know. Start with the manager of a mutual fund that specialized in stocks, says investors should consider this area only if you have a thorough understanding of the company and are doing all the required research “fun.” For example, a race-car fan might want to check out International Speedway Corp., which races events at major tracks. **LOCAL BANKS.** How else do you discover these lower profile companies? Trade publications are a good source of ideas. Local business journals often carry quotes of board stocks, most notably some of the 10,000 banks traded in the OTC market. *Walker’s Manual* lists small community banks with strong balance sheets and exceptional earnings, says Eisenberg. For example, Lancaster National Bank turned more than the average for small-bank stocks in 1995. But its stock trad-





four times earnings and of its book value at end.

Whether you choose to into an unlisted local or a company within a in industry, you can narrow your choices using the xes in *Walker's*. Here, anies are ranked by a ber of measures, including market capitalization, p-e, price-to-book value, and ound revenue growth.

nce you find a stock that ars undervalued, don't

Walker's word for it: the company. Some may ily send you information.

Others may be less cooperative—or even hostile. If so, be wary. "It's a big problem if management doesn't have any interest in husbanding the interest of minority shareholders," says Shorts.

The more knowledgeable you are, the better protected you'll be against the biggest risk associated with these investments: illiquidity. Finding buyers isn't the problem. "When shares become available, it's like throwing a handful of chicken feed into a coop: Everyone dives for it," McLaughlin says. Even more worrisome is the steep

spreads between the bid and ask prices. "Many are bid-only market orders, so the stock creeps up in price without a transaction ever taking place—as market makers try to trump each other's bid," Norberg says.

"GET RICH." Without the proper information, first-time investors may not only pay a higher price for the stock but may also get less for it when they eventually sell. "The trading aspect is so difficult it's beyond the experience of most individuals and even most brokers," says Charles Royce, who manages two closed-end mutual funds, Royce Value Trust and Royce Micro-

Cap, which hold 5% of their assets in OTC stocks. One way to protect yourself: Never put in an open order to buy at market—because you'll often end up paying more. Also, you're more likely to get a good price at the end of the month, when market makers update the pink sheets, says Eisenberg, who has 15% of his net worth in these investments.

Once investors understand the risks, they may discover what prominent value strategists such as Mario Gabelli have long understood. "These aren't necessarily 'feel-good'

stocks, where you buy them and watch them go up. But if you do it right, these really are get-rich stocks," Gabelli says. He should know. In 1993, Michael Ferrucci, director for corporate finance at Barelay Investments in Providence, heard there was a block of stock available in Providence Journal Co. Privately owned since the early 1800s, the newspaper had evolved into a multimedia conglomerate—exactly the type of media play Gabelli specialized in. Even though there was a huge spread between the bid and ask prices, he suggested Gabelli buy the shares. Three years later, the stock has returned in excess of 85%, and Gabelli believes it's still undervalued. "After going public in June, the stock is up 21%—despite the market being hammered," Ferrucci says.

Granted, few investors have Gabelli's contacts or resources. But that doesn't mean they can't learn from his experience. By sticking to an industry he knew well, Gabelli was able to ascertain that despite the big spread, the company was exceptionally undervalued.

Remember that unlisted companies are long-term plays. The stocks often don't trade every day—but then they're not subject to short-term influences. Think of it this way: You won't be tempted to watch the ticker, and your stomach won't rise and fall with the stock market, either. *Kerry Capell*

A Sampling of Unlisted Stocks

All are trading under 10 times earnings and at a substantial discount to book value.

BOSTON SAND & GRAVEL (BSND) \$181* a share. is 100-year-old producer of concrete, sand, and gravel with minimal debt and compounded earnings growth of 6%. The share price has doubled in three years—and is up 17% so far this year.

BROWN CITY PLATING (CCPG) \$7.25 a share. The 6-year-old company provides metals and plastics finishing to such companies as GM and Gillette. Compounded earnings-growth rate is 15%, and there's no debt. It's up 38% in 1996 and pays a 5.5% dividend.

GLOUCESTER BANK & TRUST (GBTR) \$60 a share. A 10-year-old Massachusetts community bank with compounded earnings growth of 81%. The stock is up 6% this year and pays a 6.6% dividend.

ST. LOUIS STEEL CASTING (STLO) \$27.25 a share. The 70-year-old foundry has a compounded earnings growth of 50% and no debt, pays a 2.5% dividend, and is up 12% this year.

*All prices are as of Aug. 2, 1996.

DATA: WALKER'S MANUAL OF UNLISTED STOCKS

PLATINUM CARDS: MOVE OVER, AMEX

During the waning days of his marriage to Princess Diana, the future King of England left little doubt as to who had become the object of his affections. The London tabloids were abuzz with rumors that Prince Charles presented Camilla Parker Bowles with an American Express Platinum Card and instructed her to charge up a storm. That she did, the papers claimed, for a new wardrobe.

You don't have to be a royal to troll around with American Express Platinum, but it helps to have a few pounds—or dollars—in the bank. Annual membership for the decade-old platinum charge card is \$300, plus \$150 for supplemental cards. The plastic is aimed at the top-spending 1% of AmEx's 36 million charge-card customers, many of whom use the elite card for business.

TEASER RATE. Now two large credit-card issuers are trying to penetrate that prestigious platinum territory. MBNA America Bank and

First USA Bank recently unveiled no-annual fee platinum MasterCard and Visas with credit lines of up to \$100,000. The MBNA Platinum Plus starts off with a teaser 5.9% annual percentage rate for purchases, cash advance checks, and balance transfers through your first five monthly statements, after which the rate climbs to the current fixed 16.9%. In some cases, MBNA Platinum cardholders can get a variable rate tagged to the prime.

You can do even better with the First USA Platinum Card, which rises from the same 5.9% to a fixed 12.99% rate in February.

The new cards have other features in common. Both provide \$1 million in travel-accident insurance, as well as emergency cash and airline tickets, year-end summaries of all your charges, and registration of all your credit cards, allowing you to report lost or stolen cards with a single toll-free call.

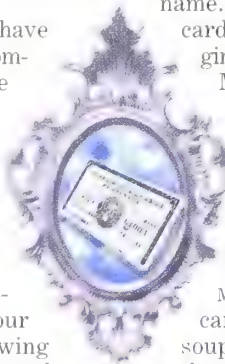
MBNA cardholders are en-

rolled in Platinum Passage, a travel service that promises its customers the lowest airfare at the time of ticketing, with agents on hand 24 hours a day to make changes to your itinerary. For an extra \$35 a year, customers can accumulate points toward free airline travel. MBNA also will give a year or nay on increasing your credit line within 15 minutes. First USA has a value-mile program in which points toward free travel are awarded each time the card is used. The \$24 annual fee is waived the first year.

Despite these benefits, industry watchers believe that American Express still outshines the competition. (In fact, an AmEx spokesperson says the company holds a trademark on the term "platinum card" and is investigating possible misuse of the name.) "I see the new cards as a marketing gimmick," says Robert McKinley, president of Ram Research Group, a credit-card market-research firm. Adds James Daly, editor of *Credit Card Management*: The MBNA and First USA cards "are more like souped-up gold cards rather than something along the lines of American Express Platinum."

Indeed, whatever prestige

its wealthy platinum customers derive from flash the card, the fact is AmEx card is a good deal those who take advantage its loftier services. Members who buy a full-fare busin-



SMART MONEY

or first-class international ticket on China Airlines; other carriers can get a companion ticket at no cost. Those who sail on certain cruise lines can earn either two-category cabin upgrade or a \$300 shipboard credit. **TENNIS ANYONE?** AmEx Platinum customers also receive invitations to exclusive events, such as a recent concert rehearsal by The Tenors and a wine tour in Bordeaux. (Members handsomely for such privileges—\$1,500 for dinner for the tenors.) They also nab court-side seats at U.S. Open Tennis Championships and earn access to special Mardi Gras parties.

Platinum holders can have American Express put a reminder in their statement for important birthdays, anniversaries, and meeting dates and a personal 24-hour concierge can arrange for delivery of hard-to-find goods with 15% discounts at select merchants as Alfred Durand and Hammacher Schlemmer. The personal consultant can help businesspeople travel overseas, locate a meeting room or arrange for an English-speaking secretary. Small business owners who opt for the corporate version of the AmEx Platinum Card, which also costs \$300 a year, receive quarterly management reports categorizing expenses.

Such royal treatment costs you plenty. But when it comes to living like a king, not all platinum is created equal.

Edward B.

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No-fee credit card with lines up to \$100,000 and 5.9% initial rate that rises to a fixed 16.9% or lower variable rate. Platinum Passage service guarantees lowest airfare at time of ticketing.

RE TRAVEL CLUBS REALLY WORTH THE FEE?

Just like shoppers who shudder at the thought of paying full retail price for an item of clothing, few vacationers expect to shell out full fare for an airline ticket or a hotel stay. Probably, it can take a fair amount of legwork to pin down the best discounts when you're planning a trip. Coming to the rescue of busy travelers is a growing number of services offering members deep discounts on air

TRAVEL

trips, cruises, car rentals, restaurants. For a membership fee of \$50 to \$144, you get telephone access to an agency that provides a variety of deals, often including last-minute ones.

TRIPS. Most clubs can knock off as much as 50% off regular rates at thousands of hotels, motels, and resorts in the U.S. and abroad. In addition to the member discounts, some give a rebate of 5% to 10% on any bookings you make through their service. So it doesn't take much to offset membership cost even if you're only an occasional traveler.

There are dozens of different clubs out there, some targeting special groups such as seniors or gamblers and others throwing in extra features such as roadside assistance. One of the leaders in the field is CUC Travel Services in Stamford, Conn., which boasts 8 million members. It not only markets its own brand, Travelers Advantage, but runs similar programs under the names of other card issuers, such as Bank and Banc One; retailers such as Sears; oil companies such as Citgo; and the e major online services.

The companies generally seek out members through direct mailings. The July, 1995, issue of *Consumer Reports Travel Letter* has a complete listing of travel clubs. To request a copy, send \$5 to the publication at 101 Truman Ave., Yonkers, N.Y., 10703.

Although the price of entry to a travel club is low, think carefully before you sign on. "It looks so good that a lot of people spend \$50 for membership they never use," says Josef Aukee, an editor at *Consumer Reports Travel Letter* in San Francisco.

"To make it worthwhile, you need to take at least two trips a year." You also have to be flexible with dates. Most discounts are only valid "subject to availability," which means there is no guarantee



you'll find a hotel room or air ticket when you need one. So a club makes more sense for retirees and adults without children than business travelers and parents tied to school schedules.

Something else to remember is that travel clubs don't have a lock on rock-bottom rates. If you're a good bargain hunter or you have a diligent travel agent, you can

snare big discounts on your own. "If you're willing to hustle, you can call hotels directly and cut a better deal than what your club is offering," says Christopher McGinnis, editor of *The Ticket*, an Atlanta-based newsletter for business travelers. Alternatively, you can go through a good airfare consolidator, cruises-only travel agency, or hotel broker to

snare big discounts. For example, the Hotel Reservations Network (800 964-6835) books rooms at preferred rates in 20 U.S. cities as well as London and Paris.

Still, the main advantage of a club is that it will do the legwork for you. "It's a one-stop shopping strategy which saves a lot of time," says McGinnis. Clubs work best for travelers who know what they want. So if all you're sure of is you'd like to take a vacation somewhere in a nice place, you're better off consulting a full-service travel agency for ideas. But if you're someone who knows where and how you'd like to travel, yet want to shave some bucks off the price, join the club. *Silvia Sansoni*

Wanderlust on the Cheap

GOLF ACCESS

800 353-4653. Annual fee: \$49.95

Targets golfers. Offers reductions on greens and cart fees as well as discounts on car rentals and cruises, but not hotels.

HIDEAWAYS

800 843-4433. Annual fee: \$99

Specializes in finding upscale vacation home rentals in exotic locations without charging a commission. Also offers 10% off some hotels and cruise lines.

SEARS DISCOUNT TRAVEL CLUB

800 548-1116. Annual fee: \$49.95

Offers last-minute deals on tours and cruises, car-rental discounts, 5% to 10% rebates on all travel purchases, and a certificate for \$40 to \$100 off an American or United Airlines ticket.

TRAVEL WORLD LEISURE

800 444-8952. Annual fee: \$50

Provides 25% to 40% discounts at upscale big-city hotels and beach resorts and 15% to 25% off airfares. Arranges deals on cruise and tour packages and offers a dining discount program.

TRAVELERS ADVANTAGE

800 548-1116. Annual fee: \$49

Offers 5% cash back on travel purchased through service; 24-hour, toll-free access to agents for bookings and information; up to 50% discount at more than 3,000 hotels worldwide, and low-price guarantee on airfares and car rentals.

DATA: CONSUMER REPORTS TRAVEL LETTER, BUSINESS WEEK

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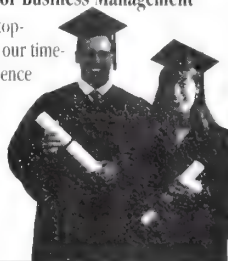
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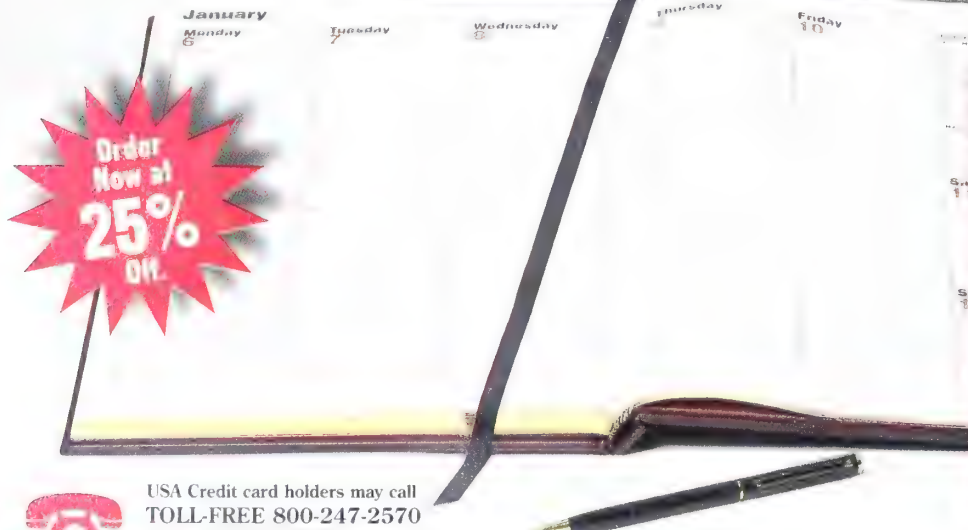
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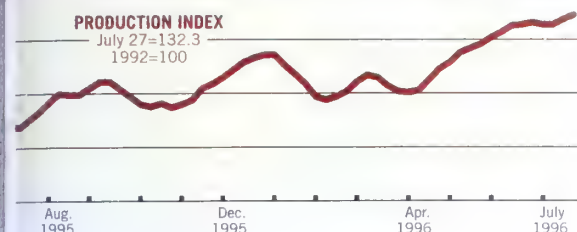
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Business Week Index

PRODUCTION INDEX

Change from last week: 0.3%
Change from last year: 7.3%



The production index edged up slightly during the week of July 27. Before the end of the four-week moving average, the index increased by a stronger 0.5% to 133.8 from 132.5. Seasonally adjusted output of trucks and autos edged back as plants reopened after the yearly shutdown for model changes. Electric power output declined in the latest week. Leading index will be unavailable for an indefinite period of time.

Production index copyright 1996 by The McGraw-Hill Companies

PRICING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (8/2) S&P 500	662.49	635.90	18.4
CORPORATE BOND YIELD, Aaa (8/2)	7.73%	7.81%	0.5
INDUSTRIAL MATERIALS PRICES (8/2)	107.3	106.8	-5.6
BUSINESS FAILURES (7/26)	NA	NA	NA
REAL ESTATE LOANS (7/17) billions	\$521.9	\$521.8	6.3
CREDIT SUPPLY, M2 (7/22) billions	NA	NA	NA
BANK CLAIMS, UNEMPLOYMENT (7/27) thous.	292	321r	-20.9

Sources: Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Street (failures of large companies), Federal Reserve, Labor Dept.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
MUTUAL FUNDS (8/6)	5.10%	5.33%	5.73%
COMMERCIAL PAPER (8/7) 3-month	5.43	5.54	5.80
CERTIFICATES OF DEPOSIT (8/7) 3-month	5.40	5.55	5.75
FIXED RATE MORTGAGE (8/2) 30-year	8.41	8.40	8.04
ADJUSTABLE MORTGAGE (8/2) one-year	6.14	6.10	5.90
LIBOR (8/6)	8.25	8.25	8.75

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

RETAIL SALES

Monday, Aug. 13, 8:30 a.m. EDT ▶ Retail sales likely slipped 0.1% in July following a dip in June, says the median forecast of economists surveyed by MMS International of The McGraw-Hill Companies. However, given the weak reports from cars and other retailers, even the smallest slip may be too optimistic. Excluding store sales likely rose 0.2% in July, advancing 0.1% in June.

CONSUMER PRICE INDEX

Monday, Aug. 13, 8:30 a.m. EDT ▶ The July core rate, which excludes food and energy prices, says the MMS report. In June,

all prices rose a mere 0.1%, and core prices edged up 0.2%.

BUSINESS INVENTORIES

Wednesday, Aug. 14, 10 a.m. EDT ▶ Inventories held by manufacturers, retailers, and wholesalers likely rose 0.2% in June. Stock levels fell 0.1% in May.

PRODUCTIVITY AND COSTS

Wednesday, Aug. 14, 10 a.m. EDT ▶ Output per hour worked in the nonfarm sector probably fell at an annual rate of about 0.5% in the second quarter, partly reversing a 2.1% gain in the first. If so, then unit labor costs likely grew about 3.5%, after rising 1.1% in the first quarter.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (8/3) thous. of net tons	2,022	1,964#	6.1
AUTOS (8/3) units	122,282	123,317r#	6.3
TRUCKS (8/3) units	105,624	107,044r#	0.0
ELECTRIC POWER (8/3) millions of kilowatt-hrs.	NA	72,804#	NA
CRUDE-OIL REFINING (8/3) thous. of bbl./day	14,299	14,092#	-1.1
COAL (7/27) thous. of net tons	19,525#	18,982	-0.8
PAPERBOARD (7/27) thous. of tons	NA#	920.0	NA
PAPER (7/27) thous. of tons	NA#	797.0	NA
LUMBER (7/27) millions of ft.	486.9#	471.0	4.7
RAIL FREIGHT (7/27) billions of ton-miles	26.4#	25.8	4.3

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Forest & Paper Association, WWP1, SFPA2, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (8/7) \$/troy oz.	388.000	385.300	1.0
STEEL SCRAP (8/6) #1 heavy, \$/ton	134.00	133.50	-6.0
COPPER (8/3) ¢/lb.	96.2	96.5	-31.8
ALUMINUM (8/3) ¢/lb.	71.0	70.0	-18.4
COTTON (8/3) strict low middling 1-1/16 in., ¢/lb	76.95	77.01	-7.8
OIL (8/6) \$/bbl.	21.46	21.43	20.0

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (8/7)	107.79	106.77	93.65
GERMAN MARK (8/7)	1.48	1.47	1.43
BRITISH POUND (8/7)	1.54	1.56	1.58
FRENCH FRANC (8/7)	5.06	5.00	4.92
ITALIAN LIRA (8/7)	1519.5	1519.2	1588.3
CANADIAN DOLLAR (8/7)	1.37	1.37	1.36
MEXICAN PESO (8/7) ³	7.494	7.576	6.150

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

INDUSTRIAL PRODUCTION

Thursday, Aug. 15, 9:15 a.m. EDT ▶ Output at the nation's factories, mines, and utilities probably dropped 0.2% in July, after jumping 0.5% in June, forecasts the MMS report. That's suggested by the declines in manufacturing payrolls and workweek. The average operating rate for all industries likely slipped to 82.9% last month, from 83.2% in June.

HOUSING STARTS

Friday, Aug. 16, 8:30 a.m. EDT ▶ Housing starts likely fell to an annual rate of 1.45 million in July, forecasts the MMS report. June starts had risen an unexpected 1.3%, to a 1.48 million pace.

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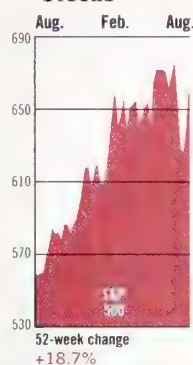
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Investment Figures of the Week

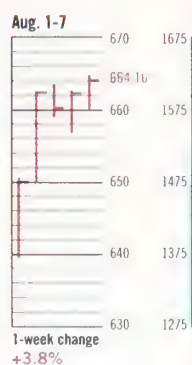
STOCKS

MONDAY
The Dow Jones Industrial Average rose 18.7% for the week in the Dow Industrials was surpassed by the S&P 500 index, which went begging just go, are now the rage. The Stanley High Tech index 8%.

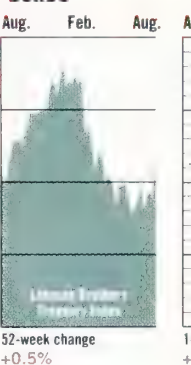
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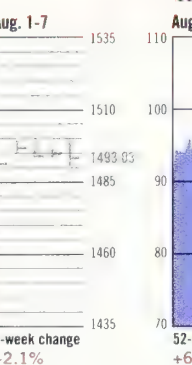
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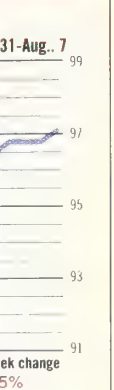
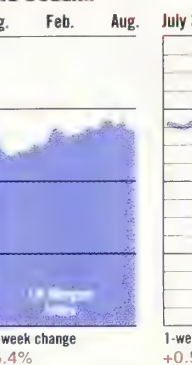
THE DOLLAR



THE DOLLAR



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
DOW INDUSTRIALS	5718.7	3.4	22.4
COMPANIES (S&P MidCap Index)	228.7	4.0	10.9
COMPANIES (Russell 2000)	327.6	3.7	9.3
COMPANIES (Russell 3000)	376.4	4.0	17.2

INTERNATIONAL STOCKS	Latest	% change (local currency) Week	% change (local currency) 52-week
FINANCIAL TIMES 100	3811.1	2.9	9.9
NIKKEI INDEX	20,477.6	-1.0	22.0
TSE COMPOSITE	5031.7	2.1	8.8

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.16%	5.30%	5.53%
30-YEAR TREASURY BOND YIELD	6.77%	6.97%	6.92%
S&P 500 DIVIDEND YIELD	2.17%	2.24%	2.38%
S&P 500 PRICE/EARNINGS RATIO	19.0	18.3	16.2

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	636.8	635.0	Positive
Stocks above 200-day moving average	54.0%	44.0%	Neutral
Speculative sentiment: Put/call ratio	0.58	0.63	Negative
Insider sentiment: Vickers sell/buy ratio	1.97	2.10	Positive

INDUSTRY GROUPS

MONTH LEADERS	% change 1-month	% change 12-month
CENTER BANKS	6.9	35.1
FINANCIAL SERVICES	5.7	30.0
MINIMUM	5.6	-3.5
OR REGIONAL BANKS	5.3	31.5
SEWAGES	5.2	10.6

MONTH LAGGARDS	% change 1-month	% change 12-month
PRIME TOOLS	-16.1	-33.8
CKING	-13.6	-36.8
ENSE ELECTRONICS	-7.8	49.4
LINES	-7.2	3.0
LISHING	-6.7	3.2

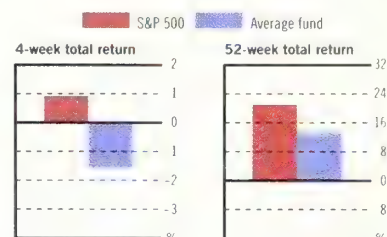
Strongest stock in group	% change 1-month	% change 12-month	Price
BANKAMERICA	9.1	53.2	82 ¹ / ₂
GREEN TREE FINANCIAL	15.8	33.8	36 ¹ / ₂
ALCOA	8.7	7.5	60 ¹ / ₂
FIRST BANK SYSTEM	10.4	45.4	62 ¹ / ₂
RUBBERMAID	7.5	-2.1	28 ³ / ₄

Weakest stock in group	% change 1-month	% change 12-month	Price
GIDDINGS & LEWIS	-27.0	-33.3	11 ¹ / ₂
CALIBER SYSTEM	-30.4	-55.8	18 ⁷ / ₈
EG&G	-8.4	2.7	19 ¹ / ₈
SOUTHWEST AIRLINES	-10.4	-13.5	24 ³ / ₄
McGRAW-HILL	-9.0	4.7	40 ³ / ₈

MUTUAL FUNDS

LEADERS	%	LAGGARDS	%
4-week total return		4-week total return	
ELITY SELECT REGIONAL BANKS	5.8	LEXINGTON TROIKA DIALOG RUSSIA	-19.4
ELITY SELECT HOME FINANCE	5.7	PREMIER STRATEGIC GROWTH B	-12.7
UDIOA	4.9	PERKINS OPPORTUNITY	-12.7

52-week total return	%	52-week total return	%
MARK SMALL CAP EQUITY A	65.3	STEADMAN TECHNOLOGY GROWTH	-34.5
NITREND GOLD	53.0	UNITED STATES GOLD SHARES	-20.3
RNER SMALL CAP EQUITY	50.0	BHIRUD MID CAP GROWTH	-19.1



RELATIVE PORTFOLIOS

Amounts represent the net value of \$10,000 invested one year ago in each portfolio.

Percentages indicate 1-year total returns.

U.S. stocks
\$12,102
+4.27%

Foreign stocks
\$11,326
+1.69%

Treasury bonds
\$10,794
+3.47%

Money market fund
\$10,526
+0.11%

Gold
\$10,110
+1.29%

Data on this page are as of market close Wednesday, Aug. 7, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are

as of market close Aug. 6. Mutual fund returns are as of Aug. 2. Relative portfolios are valued as of Aug. 6. A more detailed explanation of this page is available on request. r=revised

WANTED: STRAIGHT TALK ABOUT ENTITLEMENT

Bob Dole may be 73, but he certainly knows how to liven up an election campaign. What was fast becoming a stuporous political exercise just weeks ago could now turn into an exciting debate on economic growth, prosperity, and how to achieve them. By framing his Presidential campaign in terms of tax cuts and trust—here are 15% cuts in income taxes, and trust me to find a way to pay for them—Dole promises to leave more money on the kitchen tables of anxious American households and balance the budget to boot. We like that idea, because if Dole is serious about tax and budget reform, he must force the nation to get serious about entitlement reform.

When it comes to cutting middle-class entitlements, we've all been cowards. Faced with the need to curb the rate of growth in Medicare and Social Security, kids can't face their parents, the elderly can't face their grandchildren, Democrats turn to demagoguery, and Republicans run for cover. We want to hold Dole to his word, and we trust him to be tough enough to face his own generation.

But first, Dole must level with us. The old deficit hawk who now embraces supply-side tax cuts knows perfectly well that the plan he enthusiastically proposed on TV doesn't compute. There is no way he can take entitlements off the table, cut \$548 billion in income taxes (\$406 billion from a 15% cut in marginal rates, \$13 billion from cutting the capital-gains rate from 28% to 14%, \$75 billion from a child tax credit, \$27 billion from repealing a 1993 tax hike on Social Security benefits, and \$27 billion from expanding IRAs and credits for education and training), and still balance the budget by 2002. This is pure campaign rhetoric. Even when he uses dynamic scoring and figures that the Treasury will get back up to 27% of lost

revenues through higher economic growth, Dole can't finish his plan. He would have to take nearly \$400 billion out of small, discretionary part of the budget. In Dole'speak: "Can be done. Bob Dole knows it. American people know it."

Entitlement programs—Medicare and Social Security are the largest and fastest-growing—eat up more than half the budget. In 1962, they accounted for less than 30% of the federal budget. Throw in interest on the debt left from the 1980s, and more than two-thirds of the budget is not at discretion: It's mandated. Even without a single tax cut, the rate of growth in these entitlement programs will have to be curbed if the budget were ever to be balanced.

People know this. Poll after poll, including the latest *BUSINESS WEEK/Harris Poll*, shows that the populace favors cutting spending and bringing down the deficit over blindly cutting taxes. But people think this way only in the abstract: They can't bring themselves to force Mom and Dad to end their for-service medicine under Medicare and join HMOs, and they hesitate to cap Social Security benefits and the Cost of Living Allowance (COLA)—all of which would curb the growth of costs. And Mom and Dad sure as heck aren't volunteering to take less in order to help out their kids, much less their grandchildren, who will face enormous tax burdens.

The simple truth is that if Bob Dole's tax cuts are to be credible, he must find a credible means of financing them: cutting entitlements. What Dole should do is promise in advance to appoint a bipartisan commission on entitlement reform and pledge to abide by its recommendations. If he doesn't, voters will figure he's just as chicken as they are, his tax cuts will only generate new deficits, higher interest rates, and lower economic growth.

THE PROMISE AND PERIL OF WELFARE REFORM

There is only one honest reaction to the recent welfare bill by people in the political center—anxious anticipation. The current welfare system doesn't work, and the politicians and bureaucrats who created it over the past 60 years have been unable or unwilling to reform it. So now, a vast experiment is under way—or 50 experiments, as each state attempts to do what Washington failed to do: move people from welfare to work while protecting the young and innocent. Devolution is the new answer to welfare reform.

That's what worries us. We hope we are proved wrong, but the states have hardly been paragons of good government in the past. Education is, after all, a local responsibility, and it has gone to rot under the aegis of the states. Many legislators use patronage from school districts to get elected. Others have refused to make sure that kids unlucky enough to be born poor get the same schooling as richer kids.

What makes us think these politicians are going to solve in-

tractable welfare problems? Under the new law, half of a state's welfare recipients must be placed in jobs within three years. But with the federal government actually cutting welfare expenditures by \$56 billion, state officials will be hard-pressed to find the funds. They will have to find new funds for immigrants and find money for food stamps and Medicaid.

Our guess is that a handful of states—Iowa, Michigan, Minnesota, Wisconsin, and a few others—will do a decent job in welfare reform. They have first-rate governors and relatively clean state legislators. Other states will be tempted to "race to the bottom": cut welfare expenditures in the name of fiscal prudence and economic competitiveness.

Our best hope is for a few of the experiments to succeed and to revisit the welfare problem with new answers in the future. The states have an opportunity to deliver on the promise of devolution. In the meantime, we remain anxious like so many others—hoping for the best, fearing the worst.

ST 26, 1996

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GSM, the global standard for wireless communication, and the basis for new and exciting personal communication services, is going wide-band (64 kb/s and more). And suddenly you will be able to transmit live video through your wireless phone.

Obviously, video is of vital importance when organizing emergency relief at a big fire, traffic accident, earthquake or any situation where people on the scene need to show things very quickly to people off the scene.

Or take surveillance as another example. With traffic cameras connected through wireless phones, many more can be deployed, virtually

anywhere. Without miles of expensive cabling.

In business, you will be able to show people back at headquarters what that exhibition booth or construction site looks like. In living color.

Who knows, in a few years you may even

be sending live video postcards while on vacation – because wireless video is easily accomplished. All you'll need is a standard camera, a standard laptop computer. And your GSM wireless phone.

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All this means that there are many people who stand to benefit from GSM. Relief workers. Traffic police. Business executives.

And, of course, the occupants of apartment 16C.



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ERICSSON 



CALIFORNIA DREAMIN'
The GOP looks a little shinier,
but it's still a party divided *page 22*

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AUGUST 26, 1996



**A SWING—
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After a decade of painful downsizing and a strict focusing on productivity, Big Thinkers are back in vogue across Corporate America. But these days, strategy spinning isn't confined to the aeries of top management. The challenge: Involve workers throughout the organization, don't be bound by industry traditions, eschew incremental change, and adapt your strengths to create or redefine future markets

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Up Front



EDITED BY LARRY LIGHT WITH LISA SANDERS

POLITICS AS USUAL

A STINK ABOUT THE SUPERFUND

BARBARA WILLIAMS SPOKE to the GOP convention on Aug. 13 as a victim of overzealous regulators. Trouble is, Williams' real gripe should be with the GOP Congress, which has had two years to fix her problem and hasn't.

Williams' SunnyRay diner in Gettysburg, Pa., is ensnared in litigation involving the Superfund toxic waste cleanup program. Williams

says she sent food scraps to a private landfill that also took hazardous waste. The Environmental Protection Agency sued several large

companies to pay for a multi-million-dollar cleanup. To spread around the cost, those



LOYALIST: Diner owner Williams

companies sued hundreds of smaller fry that used the landfill, who in turn sued Sunny-

Ray and others. Although she says she has obeyed the law, her share of the cleanup could come to \$76,000.

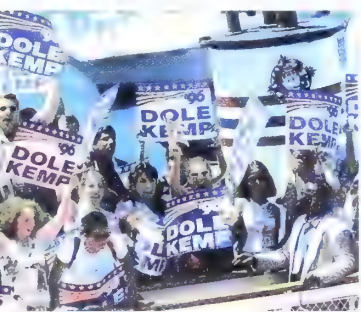
In Congress, Democrats have pushed to exempt small businesses, such as SunnyRay, from cleanup costs. They wanted to release all businesses from liability for 1987 dumping, but could agree on how to pay for broad relief. Still, Republican Williams won't bash her party. "At least they invited me to speak."

Mary Regan and Joseph Weber

CAMPAIGN COFFERS

DOWN AND OUT IN SAN DIEGO

THROUGHOUT THE GOP convention, delegates flourished thousands of bright blue-and-red signs reading "Dole-Kemp '96." The signs' small print read: "Paid for by Jack Kemp for Vice



DOLIES: "Perfectly legal"

President Committee." That marks the latest clever trick the Dole camp has used to get around Federal Election Commission spending limits. In order to boost spending at the convention, Bob Dole's campaign created a new political committee on Aug. 7 to pay for the signs, plus Kemp's staff, hotel, and other costs. The tab's unknown, yet likely is in the tens of thousands. "This is perfectly legal," says Dole spokeswoman Christina Mar-

tin. Certainly, it's a loophole. Earlier, Dole used creative accounting to transfer expenses from his cash-strapped primary to his general-election fund.

For a budget-cutter, Dole has had problems staying under the spending ceiling. He hit the \$37.1 million primary-season cap early. The Dems have filed a complaint with the FEC, saying Dole was over by \$342,000 in May. But Dole's money woes are over. Once he was nominated, he qualified for \$62 million in public funds. Mary Beth Regan and Richard S. Dunham

HONCHOS

NO GENERAL AT GENERAL MOTORS

BOB DOLE ISN'T the only suitor who has been rejected lately by Colin Powell. Besides turning down the No. 2 spot on the GOP ticket, the retired general recently declined an offer to join the General Motors board, say people close



POWELL: Thanks, but...

to the automaker.

GM, which has only one African American on its board, courted Powell intensely. A principal recruiter was

Harry Pearce, who served the Howard University board of trustees with Powell. Chairman Jack Smith made a personal pitch to the gulf war hero, the insider says. But the perks of a big seat at General Motors (\$26,000 annual retainer, stock grants, other benefits) were hardly enough to lure the general.

Powell doesn't exactly need the money: He earned a fortune from his bestselling autobiography and demands a speaking fee of \$65,000. The general could not be reached, and GM declined comment. GOP consultant Kenneth Duberstein, a close Powell associate, will say only that Powell has received dozens of requests to join corporate boards and said no to all. Bill V.

THE LIST ELECTORAL MATH

From 1968 through 1988, the GOP benefited from its 21 "lock" states. This bloc was vital to victories in five of the six Presidential races. Then, in 1992, Clinton took nine lock



states. If Dole can regain them — especially California — and win George Bush's '92 states, he'll have 286 electoral votes, with 270 needed for victory.

GOP "LOCK" STATES DOLE MUST WIN BACK

Electoral Votes		Electoral Votes	
CALIFORNIA	54	NEW HAMPSHIRE	4
COLORADO	8	NEW JERSEY	15
ILLINOIS	22	NEW MEXICO	5
MONTANA	3	VERMONT	3
NEVADA	4	TOTAL	118

DATA: CONGRESSIONAL QUARTERLY

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QUAYLE'S SPELL IN PHOENIX

FORMER VICE-PRESIDENT DAN Quayle is pulling up stakes in Indiana this fall to relocate to Phoenix, where he'll teach international affairs at the Thunderbird School of Management. The ex-Veep disclosed his plans to San Diego conventioners at a party he hosted.

Quayle, who briefly flirted with a 1996

Presidential run, spent some of his teens in Phoenix, where his family publishes *The Arizona Republic*. After the '92 election, Quayle and wife Marilyn returned to suburban In-



OUT OF INDIANA: Quayle

dianapolis. Now, their Carmel home is for sale. Marilyn, an attorney, plans to commute.

A big Phoenix plus for ardent golfer Quayle, says a friend, is that "he can play all year round." Since leaving D.C., Quayle has been raising money for the party and writing books.

He didn't bring his clubs to San Diego, though flooded with golf invites, friends say. Reason: to avoid turning down people he'd need for a 2000 run. *Owen Ullmann*

NETWORKING

CHRYSLER'S SOUPED-UP SIDESHOW

CHRYSLER MAY BE NO. 3 among U.S. auto makers, but it emerged No. 1 in its class in San Diego. Archrival General Motors, despite being the official car provider (320 lent to dignitaries), settled for hosting a luncheon in the San

to the present. A 1930s-era display included a mock-up of a vintage Texaco service station. Chrysler also showcased its recently unveiled retro hot rod, the \$35,000 purple Prowler, on a dais in front of the hall.

The exhibit became the venue for nonstop parties with lavish food and an open bar. Chrysler Chairman Robert Eaton held a salute to Michigan Governor John Engler. Then came events honoring the GOP freshman class, as well as officeholders from states with Chrysler plants, such as Ohio Governor George Voinovich and Wisconsin Governor Tommy Thompson.

The performance underscored what many observers already knew. Chrysler, which battled back from near-collapse in the 1980s, "is better at showmanship," says auto marketing consultant Susan Jacobs. During the Democrats' Chicago convention on Aug. 26-29, Chrysler will reprise the show at Navy Pier. □

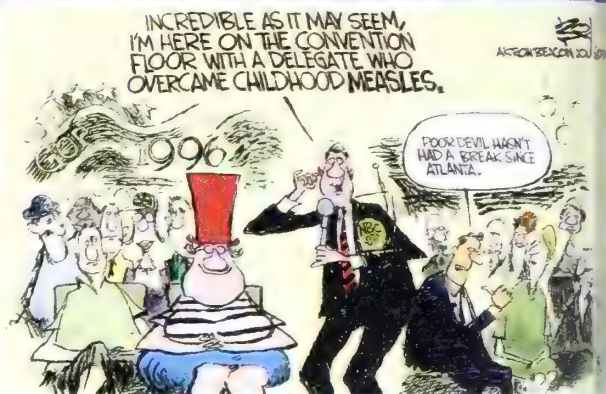


CAR TALK? Engler, Eaton

Diego Civic Center. Ford wasn't even there, for unspecified reasons.

Then there was Chrysler. A 40,000-square-foot parking garage next to the convention center became a softly lit exhibition hall featuring a collection of models from 1924

DRAWN & QUARTERED



PARTY LINES

GET ME REWRITE!

BOB DOLE IS COUNTING ON HIS tax-cutting economic plan to strike a chord with average Americans. But the drafters of the economic plank for the Republican platform seemed a bit tone deaf. Members of the party Platform Committee, chaired by Representative Henry Hyde of Illinois, were aghast to see a draft that read more like a doctoral thesis than an agenda aimed at grassroots voters.

The economic section had few references to creating jobs and to worker anxiety. Instead, it dwelt on Federal Reserve Board monetary policy, Mexican government corruption, trading partner China's use of prison labor—there was even an antiabortion pro-

posal. "We did a terrible at bringing it down to the average person," grumbled California Attorney General Lungren, head of the committee's economics panel.

So Lungren's group chucked the draft and rewrote the plank in an afternoon. The rush job had its



EASY DOES IT: Hyde (right)

problems: It was full of typos and missing letters and dropped words. The fixes were made in time for the final report. "We are great thinkers but bad typers," Lungren laughed. *Richard S. Dunlap*

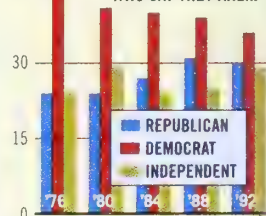
THE BIG PICTURE

PARTISAN UPS AND DOWNS

After seeing an erosion for four Presidential election years in how voters identify themselves, the Democrats are holding their own. The ranks of non-affiliated voters have fluctuated with various

political trends, such as Ross Perot's splashy 1992 crusade.

PERCENTAGE OF ADULTS WHO SAY THEY ARE...



AVERAGE OF MONTHLY PHONE SURVEYS OF 1,000 ADULTS. NUMBERS DO NOT INCLUDE "NOT SURE" OR "OTHER."



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KEY INSIGHTS INTO SHORT-SELLING

Specialized expertise—particularly medical expertise—is not unique to short-sellers (“The secret world of short-sellers,” Cover Story, Aug. 5). Virtually every Wall Street brokerage firm employs one or more former physicians or scientists as research analysts to evaluate biotechnology and health-care stocks. So do many “long-only” investment institutions, including Dreyfus Corp. and Alliance Capital Management.

Great investment research—both on the long side and on the short side—results from leveraging that expertise with shoe leather. Emotional responses, such as those of the short-sellers who “despise” and brokerage analysts who “love” a particular stock, can trip up even the most diligent analytical efforts.

Teena L. Lerner
Riverdale, N.Y.

Short-selling, like long-term investing, is nothing more than taking a position on a security—based on an informed opinion—and waiting to see if you’re on the right side of the trade. It is for this reason that regulatory agencies spend countless dollars ensuring that brokerages include the key phrase: “There may be a loss of capital trading securities” in every disclosure document, whether account application form, advisory newsletter, or fund prospectus.

M.J. Rollo
Senior Investment Strategist
International Offshore Investments
Group Inc.
Vancouver, B.C.

Heavy short-selling shifts the supply curve to the right, so it crosses the demand curve at an artificially low price. That’s how short-selling hurts stock prices. If shorts try to close their positions all at once, there isn’t enough stock and the price goes ballistic. That’s how it causes price volatility. We don’t need anybody monkeying with the supply curve. The article was an annoying

whitewash of an unnecessary practice.
Erwin Aldinger
Glen Mills, Pa.

PRESERVATION, SURE, BUT AT THE RIGHT PRICE

Maxxam Inc., its Pacific Lumber subsidiary, and Charles E. Hurwitz willing to make Headwaters Forest a 1,500- to 1,700-acre buffer zone available for public preservation, so long as there is just compensation for its guaranteed by the Fifth Amendment to the Constitution (“Save California’s redwoods—but not this way,” News: Analysis & Commentary, Aug. 5).

Recognizing the high value of the property, Maxxam, Pacific Lumber, and Hurwitz have made clear their willingness to be creative and flexible in terms of the compensation.

A swap of assets that, together, constitute just compensation is the way to preserve Headwaters.

Robert W. Ingle
Vice-President, Public Relations
Maxxam Inc.
Houma, La.

GET THE U.S. UP TO SNUFF ON BOMB SLEUTHING—NOW

In your article “Where are the bomb sniffers?” (Science & Technology, Aug. 5), John W. Wood Jr., president of Termedics Inc., says that it is ironic as someone wishing to be screened by the latest American explosive-detection technology must fly out of a European airport. I believe “despicable” or “shameful” are the more appropriate words.

Such inconsistencies in antiterrorism policy are inexcusable. It is unbearable that such luggage-screening devices are not used at U.S. airports. Public opinion in the U.S. must pressure the government to follow its European counterparts in exhausting preventative measures to prevent terrorism.

Pedro Macias
Monterrey, Mexico

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IRRECTIONS & CLARIFICATIONS

ng ultraviolence to parasites" (Developments to Watch, July 15) erred in saying ultraviolet light has not been used to drinking water.

He's a one-man radio band" (Media, 19), a photograph in the office of SFX Broadcasting Chairman Robert F.X. Sillerman is described as being of him, nude, in a bathtub. Although no clothing was visible in the photograph, other photographs in the same session show that Sillerman is wearing a blue and white bathing suit.

table accompanying "Are travel clubs really worth the fee?" (Personal Business, 19) listed an erroneous telephone number for Golf Access. The correct number is 800 359-4653.

TIME TO JETTISON CORPORATE JETS

The cost of operating a \$35 million corporate jet is near \$10,000 per hour or more, including depreciation, pilot salaries, and insurance ("An updraft for corporate jets," News: Analysis & Commentary, Aug. 5). Depreciation alone is \$7 per hour.

Aircraft manufacturers and corporate executives do not want shareholders and employees to know the cost of their jets. There is simply no justification for owning a corporate plane. If one is needed, the best solution is to charter equipment.

Frank C. Wilson
President
International Management
Gainesville, Ga.

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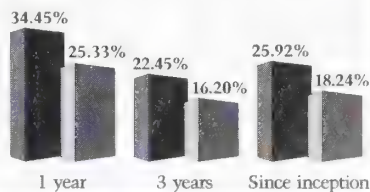
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CITIZEN PEROT

His Life & Times

By Gerald Posner

Random House • 400pp • \$25

A WILD CARD— BUT NO JOKER

Ross Perot, the towering midget of American politics, can't be summed up in a sound bite. He's one of the most complex, colorful, crafty figures on the American stage today. He has made billions of dollars as a pioneer in data processing and real estate but has lost millions in naive and ill-fated business ventures. He's a savvy and skillful business operator; yet a new book by Gerald L. Posner cites former colleagues who describe Perot as "squirrelly" and "paranoid." Perot, in turn, defiantly tweaks his critics by dancing in public to Patsy Cline's famous rendition of *Crazy*.

In *Citizen Perot*, Posner frequently does a brilliant job of capturing the contradictions of the complicated businessman-turned-politician that is Ross Perot. As portrayed by Posner, the Texan can be selflessly generous to employees needing medical help, yet he can reduce loyal workers to tears through vicious tirades. He drove a rental car to a Presidential debate yet had bulletproof sedans built for him to use during the campaign. He rails against the influence of Washington lobbyists yet hired the best lobbyists to help him secure business deals in Texas and around the world. A memorable description is found in an interview with Ken Riedlinger, a longtime executive of the company that made Perot a billionaire, Electronic Data Systems Corp.: "I like Ross. He saved my life a couple of times. But I also hate Ross. Yet I voted for him. And I would probably go back to work for him tomorrow if he asked."

Such mixed messages are central to Posner's generally balanced biography of the Dallas entrepreneur. Perot is a man whose successes and failures are the stuff of legend. And Posner carefully tries to separate fact from myth in a crisply written book that flows effortlessly from anecdote to anecdote while

never straying far from its central focus on Perot's complex character.

Posner, whose previous books include an examination of John F. Kennedy assassination theories, *Case Closed*, and a biography of fiendish Nazi doctor Josef Mengele, retells the familiar Perot tales—the rescue of his EDS employees from Iranian chaos in 1979, his messy battles with General Motors boss Roger B. Smith, and his two-decade crusade on behalf of U.S. prisoners of war in Vietnam. But Posner adds just enough new tidbits to keep the narratives from being rehashes of previous books. His interviews about Perot's daring Iran mission—including discussions with participants and former Carter Administration officials—add significantly to the historical record.

There are two major revelations in the book. One is Perot's assertion that Vice-President Al Gore had "something glistening in his ear" during their debate over the North American Free Trade Agreement, generally viewed as a triumph for Gore, who goaded Perot into embarrassing fits of temper. Perot won't provide Posner with the source for this information that Gore "cheated" in the debate but says he heard about the scheme from "word on the cocktail circuit." Democratic operatives dismiss the allegations as Perot-noia. Posner presents the incident without commentary and permits the reader to decide.

Posner also investigates Perot's controversial allegation that Republican operatives attempted to disrupt his daughter's wedding—which Perot has cited as the reason for his temporary withdrawal from the 1992 Presidential campaign. The author elaborates with what

reads like an episode of the *Keystone Kops* as viewed by a conspiracy theorist. Using interviews with all of the participants, Posner neutrally tells a bizarre tale in which a man named Sebastian Barnes—a shadowy operative who has previously worked with Perot on behalf of Vietnam War POWs—shows up on the doorstep of a Bush campaign office purportedly with dirt on Perot. The Bush aide, Jim Oberwetter, appears baffled and nervous. At Barnes's suggestion, the two men walk outside, where a hidden camera filmed the meeting. "Oberwetter was so nervous that when he saw a woman fiddling with a pack of cigarettes, he wondered if the pack had a tiny camera," Posner writes. So, Oberwetter is the target of an FBI sting operation. In the end, the feds found no wrongdoing by GOP operatives. But Perot remains convinced that his campaign was victimized by Republican dirty tricks. While the incident has been recounted before, Posner fleshes it out

with superb detail and psychological insights into the central characters.

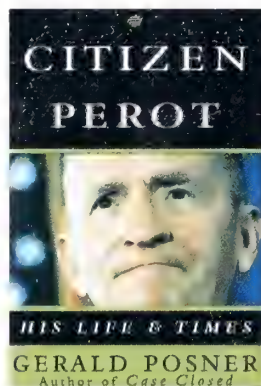
While *Citizen Perot* is meticulously researched, the book also contains a number of factual errors that will make Texas and Arkansas historians cringe. Among them: misidentifying legendary Texas politician W. Lee "Pappy" O'Daniel as an Arkansas senator and misspelling the names of former Texas

Governor Price Daniel and ex-Clinton White House Chief of Staff Thomas "Mac" McLarty.

As Perot's new Reform Party gathers to ratify its nominee on Aug. 18 in Valley Forge, Pa., some of its members say Perot is not the right man to take their third party to the next level. They'll find plenty of ammo in Posner's account. But diehard Perotistas, too, will find much here to bolster the case for Boss Ross. Posner doesn't forecast the fate of a second Perot Presidential candidacy. But his well-written biography proves that the quirky Dallas billionaire is the most unpredictable candidate in the 1996 Presidential field.

BY RICHARD S. DUNHAM

Dunham covers Capitol Hill for BUSINESS WEEK



POSNER EVENLY DISSECTS THE CONTRADICTIONS OF PEROT: HERO, SPOILER, IDEALIST, TYRANT

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THE BUSINESS WEEK BEST-SELLER LIST

HARDCOVER BUSINESS BOOKS

- 1 THE DILBERT PRINCIPLE** by Scott Adams (HarperBusiness • \$20) *The revenge of the cubicle dwellers.*
- 2 WALL STREET MONEY MACHINE** by Wade B. Cook (Light-house Publishing • \$24.95) *Formulas to help you strike it rich.*
- 3 BEYOND REENGINEERING** by Michael Hammer (HarperBusiness • \$25) *In the "process-centered" workplace, everyone is a professional.*
- 4 THE MOTLEY FOOL INVESTMENT GUIDE** by David and Tom Gardner (Simon & Schuster • \$24) *An online investment duo puts it in writing.*
- 5 CLICKING** by Faith Popcorn and Lys Marigold (HarperCollins • \$26) *Spotting trends in order to achieve success and personal fulfillment.*
- 6 INSIDE THE TORNADO** by Geoffrey A. Moore (HarperBusiness • \$25) *Lessons on marketing mined from Silicon Valley.*
- 7 BUILT TO LAST** by James C. Collins and Jerry I. Porras (HarperBusiness • \$25) *How 3M, Wal-Mart, Procter & Gamble, and others became standouts.*
- 8 THE LOYALTY EFFECT** by Frederick F. Reichheld (Harvard Business School • \$24.95) *How loyalty between management and employees spurs company growth and profits.*
- 9 CUSTOMER-CENTERED GROWTH** by Richard Whiteley and Diane Hesson (Addison-Wesley • \$25) *Overcoming adversity by putting your customers' desires at the heart of things.*
- 10 THE SECOND CURVE** by Ian Morrison (Ballantine • \$25) *Successfully confronting new technologies, new consumers, and emerging markets.*
- 11 THE DIGITAL ECONOMY** by Don Tapscott (McGraw-Hill • \$24.95) *How the Infobahn is changing business.*
- 12 CO-OPETITION** by Adam M. Brandenburger and Barry J. Nalebuff (Currency • \$24.95) *Game theory and strategy for a world of changing business rules.*
- 13 MANAGEMENT OF THE ABSURD** by Richard Farson (Simon & Schuster • \$21) *The paradoxes of management, as seen by a psychologist.*
- 14 JAMMING** by John Kao (HarperBusiness • \$23) *A guide for prompting jam sessions of creativity and improvisation.*
- 15 THE PATH** by Laurie Beth Jones (Hyperion • \$16.95) *How to plot your own mission statement.*

PAPERBACK BUSINESS BOOKS

- 1 THE SEVEN HABITS OF HIGHLY EFFECTIVE PEOPLE** by Stephen R. Covey (Fireside • \$12) *Habitually popular.*
- 2 GET A FINANCIAL LIFE** by Beth Kobliner (Fireside • \$11) *Hey, Gen X'ers—mutual funds and mortgages can be fun!*
- 3 1001 WAYS TO REWARD EMPLOYEES** by Bob Nelson (Workman • \$8.95) *Give them a champagne brunch, a casual-dress day—or plain old cash.*
- 4 THE BEARDSTOWN LADIES' COMMON-SENSE INVESTMENT GUIDE** by the Beardstown Ladies Investment Club with Leslie Whitaker (Hyperion • \$10.95) *Recipes for Four-Bean Salad, Five-Hour Stew—and 23% returns.*
- 5 THE 1996 WHAT COLOR IS YOUR PARACHUTE?** by Richard Nelson Bolles (Ten Speed Press • \$14.95) *The enduring job-search bible.*
- 6 LEARN TO EARN** by Peter Lynch and John Rothchild (Fireside • \$13) *Capitalism for beginners.*
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- 11 THE ONE MINUTE MANAGER** by Kenneth Blanchard PhD and Spencer Johnson M.D. (Berkley • \$9.95) *Three management techniques, conveyed in brief story form.*
- 12 PERSONAL FINANCE FOR DUMMIES** by Eric Tyson (IDG Books • \$16.95) *Lighthearted primer.*
- 13 YOUR MONEY OR YOUR LIFE** by Joe Dominguez and Vicki Robin (Penguin • \$11.95) *To achieve financial independence, restructure your life.*
- 14 JESUS CEO** by Laurie Beth Jones (Hyperion • \$10.95) *That team-builder and turnaround artist from Nazareth.*
- 15 HOME BUYING FOR DUMMIES** by Eric Tyson and Ray Brown (IDG Books • \$16.99) *Ah, home, sweet mortgage.*

BUSINESS WEEK's Best-Seller List is based on a survey of chain and independent booksellers that carry a broad selection of books on economics, management, sales and marketing, small business, investing, personal finance, and careers. Well over 1,000 retail outlets nationwide are represented. Current rankings are based on a weighted analysis of unit sales in July.

HOT TYPE

"PEOPLE OF THE SAME TRADE SELDOM MEET together but the conversation ends in a conspiracy against the public or in some diversion to raise prices," observed classical economist Adam Smith. Well of course, Adam M. Brandenburger and Barry J. Nalebuff might respond—that's just "co-opetition."

It's not that these "conspirators" have ceased being rivals. Rather, it's that "there is a duality in every relationship—the simultaneous elements of cooperation and competition," explain the authors of *Co-opetition* (Currency/Doubleday), No. 12 on this month's BUSINESS WEEK Best-Seller List.

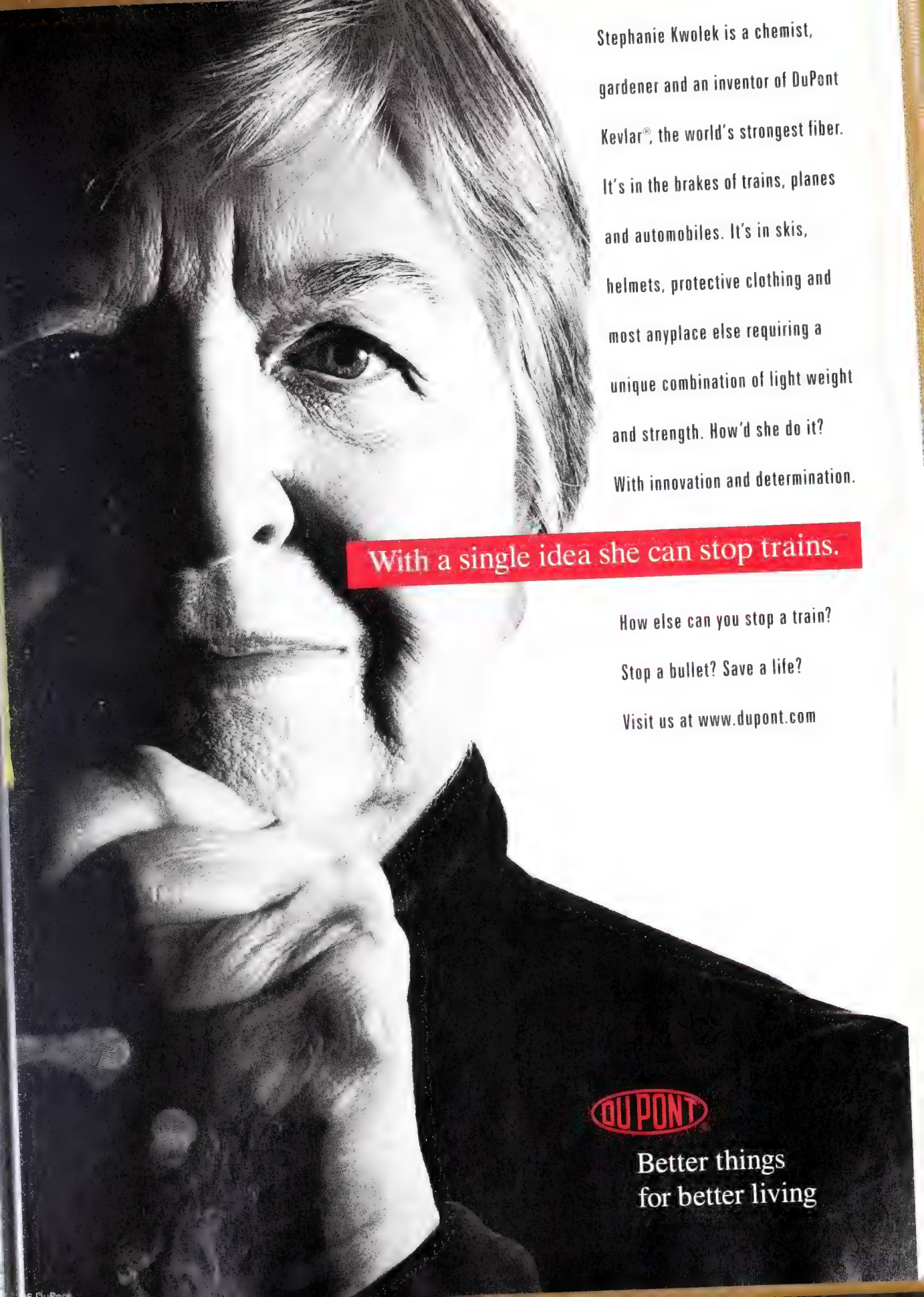
At times, a competitor may be a "complementor," particularly when working together can expand the size of a market.

And at times, a supplier or a complementor (what French mustard is to Oscar Mayer franks) can become a competitor. Everything depends on the situation—and how you can understand and shape it to your advantage.

To illuminate this way of thinking, the authors delve into game theory and provide exercises that will agitate your gray matter. They also examine each of the five elements of a game: the players, added values ("what each player brings to the game"), rules, tactics, and the boundaries of the game.

Will *Co-opetition's* games replace Parker Brothers' Monopoly? Afraid not. The book's case studies are for real—and lots more useful.

BY HARDY GREEN



Stephanie Kwolek is a chemist,
gardener and an inventor of DuPont
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BY STEPHEN H. WILDSTROM

'VCRs' FOR THE WEB

Offline Web readers fetch data when you can't, so you can surf at your leisure

Someday, we'll all browse the World Wide Web over cable modems or high-speed digital lines, so we won't have to wait forever for pages to download. Someday, Internet service providers will add enough capacity to eliminate busy signals. Someday, you'll be able to connect to the Net easily from a hotel or even a plane.

That day is still a ways off, though. In the meantime, a new breed of software gives you what I like to think of as VCRs for the Web. The programs are offline Web readers, which you instruct to go onto the Web automatically to download pages. Then, you surf through copies stored on a disk drive.

The most obvious use of these programs is to make it quicker and easier to browse through sites you visit regularly. Say you like to start your day with the scores and news from ESPNET SportsZone (<http://espnet.sportszone.com>). If your offline retriever fetches the data in the wee hours, you can scan the news as quickly as your hard drive can deliver pages.

That's only the beginning. Perhaps you need to bone up on a big customer by reading its Web pages in advance of a sales call. You can't connect to the Internet from a plane, but with an offline reader, you can download the pages and peruse them while

you fly to your appointment. Suppose you want to share with a client information available only on your company's internal Web server. Let your computer do the work, and use the pages in your presentation.

All of the offline readers work more or less the same way. Pick the sites and specify when—and how often—data should be checked. You might want to refresh a news site such as CNN Interactive (<http://cnn.com>) hourly but fetch an online magazine such as Microsoft's *Slate* (<http://www.slate.com>) weekly.



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The programs come with a menu of popular sites pre-configured for downloading, but getting the maximum benefit takes some work. The trickiest decision is determining how much data you want, specified by how many levels deep you want to follow links at each site. Go too deep, and you'll stay online for hours downloading many megabytes of data, though all the programs let you set overall limits on the amount of disk space your downloads can consume. Go too shallow, and you'll find you don't have that page you really need.

WebEx was my clear favorite among the three programs I tried. It runs entirely within either Netscape Navigator or Microsoft Internet Explorer, and was the easiest to set up. Once you launch the WebEx "agent," you type in the address of a site or make a selection from your customized WebEx home page. If the page you want is not stored in your computer, the program offers to connect to the Internet to retrieve it.

OM-Express offers similar features, but I found setting up its download schedule more difficult. FreeLoader is literally free, but you must go through a home page cluttered with ads. The program, which works only with Netscape browsers, hinders navigation by displaying a file name it invented, not the actual Web address, for pages it has stored. In addition to these programs, I've looked at test versions of WebMirror Personal from Mobileware and WebClip from PaperClip Software, interesting newcomers that should ship soon.

Beyond the obvious advantages, these programs represent a great trend for consumers. Both trial and inexpensive full versions can be downloaded, making it a low-risk proposition to give these offline readers a try.

BULLETIN BOARD

COLOR PRINTERS

QUALITY SANS SPEED

If you want color printing and have more time than money, the new Color JetPrinter 205 from Lexmark International (800 891-0331) may be for you. The printer, which works only with Windows, features separate black- and color-ink reservoirs—important for high quality and economy—and resolution of 600 dots per

inch, all for under \$300. The Color Jet



is relatively slow, taking several minutes to do a top-quality full-color page. And your computer will slow down significantly while it prints. Unlike more costly printers, this one uses the processing power of your PC rather than its own chips and memory.

PHOTO IMAGES

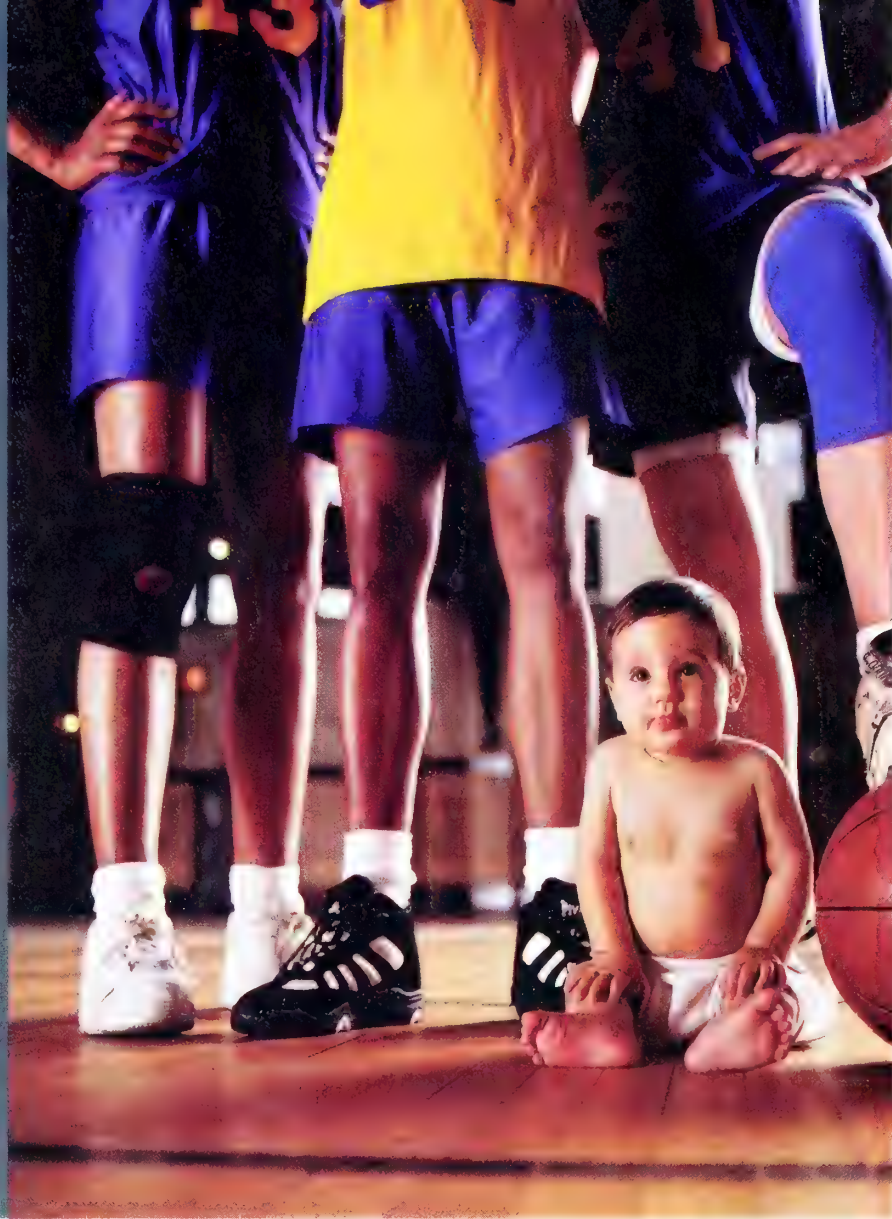
WACKY SNAPSHOTS

Computers are great at editing images, whether fixing a snapshot's "red eye" or creating a composite scene that never existed. But Kai's PowerGoo for Windows or Macintosh from Meta Tools (805 566-6200) can be just plain fun. The brainchild of Kai Krause, who is responsible for most of the special effects in high-end programs such as PhotoShop, the \$50 PowerGoo allows you or your children to fingerprint with your picture. Easy-to-use controls let you stretch, blur, and otherwise distort features. The program can record your creativity, then play the process back as an on-screen movie.

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BY GARY S. BECKER

WHY THE DOLE PLAN WILL WORK



LOGICAL:
Voodoo, the plan isn't. The tax cut's growth dividend might cover even more than the 27% of lost revenue that Dole now projects

I was surprised when I received a phone call in early May to attend a meeting in Washington with then-Senate Majority Leader Bob Dole of Kansas, other senators, and a few economists to discuss the formulation of an economic program for the Presidential campaign. I had been the consummate Washington outsider: I declined all invitations to testify before Congress and had never even set foot in the Capitol, the building where the meeting was to take place!

But I accepted this invitation because I believed that new economic initiatives were much needed to raise the growth rate of America. The meetings with Dole and his advisers gave me a priceless education on the mix of economic and other factors that determine an economic program.

It was early agreed that cuts in income and capital-gains taxes were to be the centerpiece of his program. I believed large cuts were essential; their precise form mattered much less. Dole chose a 15% across-the-board tax cut from several alternatives because families can easily understand how that would directly affect them. Moreover, this cut is a major step toward the reforms he promised for his first Presidential term: a simpler and flatter tax structure, a balanced-budget amendment to the Constitution, and the requirement of supermajorities in Congress to raise income-tax rates.

From the beginning, Dole wanted major education and training initiatives because he recognizes that investments in human capital are essential to robust long-term growth in modern economies that depend on knowledge, skills, and information. Better education and training will also help narrow the inequality in earnings that has grown over the past two decades.

VOUCHERS AND SAVINGS. His program advocates scholarships, or vouchers, for students from middle-class and poor families that could be spent at private schools, including parochial schools. Poorer students attend the worst public schools, since they cannot afford either private schools or good suburban schools. Vouchers, choice, and competition among schools sharply distinguish Dole's approach from President Clinton's, since he, along with the teachers' unions, has strongly opposed school vouchers and choice.

The Dole plan includes education savings accounts that allow families to contribute \$500 per year to an "education individual retire-

ment account" for each child, which can be spent eventually on college or other post-high school education. It also gives tax incentives to companies to pay for training and retraining employees—including those who lost their jobs possibly because of downsizing.

The Dole program plans to first stop and then roll back the rapid growth in regulation under Presidents George Bush and Bill Clinton. The Clinton Administration itself estimated that the cost of complying with federal regulations in 1995 absorbed almost 10% of gross domestic product, and the cost is continuing to rise. Dole would require benefit-cost analysis to justify new regulations and would reevaluate all existing regulations.

FEEDBACK. I believe the full program could reach the target of 3.5% growth per year. The U.S. and many other countries have enormous reservoirs of skills that are throttled by high taxes, excessive regulations, and failure to properly educate and train much of the workforce. Any country will gain a large boost in economic vitality if it can improve opportunities for men and women to start businesses and encourage much greater investments in human and physical capital.

The tax cuts and other incentives in the Dole program would reduce federal revenue by about \$550 billion over the six-year period to the year 2002. Faster economic growth and reallocation of assets toward more taxable forms induced by the whole program, not just the tax cuts, is assumed to recover during this six-year period about 27%, or \$150 billion, of the revenue loss.

I consider this 27% feedback conservative. Martin S. Feldstein of Harvard University has estimated that the 1986 tax cuts yielded 40% feedback. More than \$200 billion, rather than the assumed \$150 billion, will be recovered in six years if the Dole package raises growth by only 0.2 percentage points each year for six years. Instead of growing at 2.2% each year, the economy would grow at 2.4% the first year, 2.6% in the second, and so on.

Some critics label the assumption of revenue recovery voodoo economics revisited, but to me it is a simple implication of elementary economics taught to freshmen: that powerful changes in incentives have powerful effects on behavior. Economists should go out of business if they deny that taxes, prices, and costs significantly alter behavior. This is the strength of Dole's economic plan.

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BY GENE KORETZ

THE MIRAGE OF ZERO INFLATION

It looks good but could hurt growth

Thanks to Alan Greenspan's Federal Reserve, inflation is currently running below 3% on a year-to-year basis, a 30-year low. Yet some economists and policymakers want to go further and pursue the elusive target of zero inflation. Senate Republicans have been pushing legislation to change the Fed's official mandate from promoting high employment and stable prices to the single goal of achieving price stability.

The benefits of an inflation-free economy could be significant. Inflation breeds uncertainty, adds to borrowing costs, and hurts those living on fixed incomes. Since taxes bite into nominal rather than real investment income, it also distorts saving and investment.

But zero inflation, observe Brookings Institution economists George Akерlof, William Dickens, and George Perry in a new study, also embodies costs. And these, they find, could exact a heavy

ing morale) or making do with fewer workers. Yet evidence from labor contracts, industry data, and company and worker surveys indicates that employers almost never cut nominal wages—a reluctance apparent even during the Depression, when prices were falling.

Given that reluctance, the authors find that companies in an inflation-free economy would keep relative wages too high and employment too low, with large negative spillover effects on the overall economy. According to their econometric model, the costs of maintaining zero inflation would be a permanent drop of from 1% to 3% in employment—and a similar continuing loss in gross domestic product. "Complete price stability," they say, "should not be the Fed's goal."

A WEAKER GERMAN UPTURN

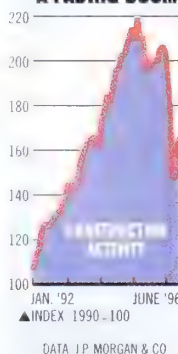
Construction in the East slows

As Germany's economic revival evolves into a sustained recovery, it is losing a significant tailwind. East German construction, which boomed in the wake of reunification, is set to decline.

Given the poor state of its building stock and the size of west German tax subsidies, it's no surprise that east German construction activity more than doubled from early 1992 through early 1995, accounting for some 15% of gross domestic product. Indeed, in contrast to the rest of the east German economy where no net jobs were created, construction employment rose by more than a third over the same period.

Now, however, the construction bubble has burst, reports economist Jörg Henzler of J.P. Morgan & Co. Building activity in late spring was 24% below its early 1995 peak. Although some of that reflects the harsh winter and will be reversed, Henzler predicts that the combination of an oversupply of new apartments and falling tax subsidies should cut housing activity in the east by an additional 20% to 30% over the next few years. That's enough, he says, to subtract as much as 0.2% from Germany's overall growth rate.

EAST GERMANY: A FADING BOOM



1997 PAY HIKES WILL STAY LEAN

But job angst may prevent whining

Labor shortages may be cropping up sporadically around the U.S., but there are still no signs that Corporate America is growing less adamant about maintaining wage restraint. A Conference Board survey of more than 60 companies, for example, finds that the median budgeted salary increase for 1997 is just 4%. That's the same number as in 1996 and the lowest level in the survey's 20-year history.

Similarly, the consulting firm William M. Mercer Inc. reports that the average raise projected for next year by some 2,300 companies recently surveyed is 4.1%, the same as in 1996. Since hitting 5.5% in 1990, notes the consultant, the size of salary hikes has been declining steadily.

One trend that may inhibit employee discontent over the modest size of salary increases is the continuing specter of large-scale downsizing. Challenger, Gray & Christmas Inc., an outplacement firm that keeps tabs on substantial corporate layoffs, reports that nearly 42,000 job cuts were announced in July, up 80% from last year's level. So far in 1996, the tally is 312,356, some 33% over 1995.

FRONT-END GROWTH IN 1996?

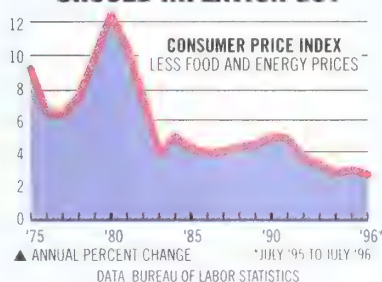
Some intriguing echoes of 1984

Like many of his fellow economists, Lacy H. Hunt of HSBC Securities Inc. believes that the economy will slow significantly in coming months. But among his reasons is one that others may have overlooked: an intriguing parallel between 1996 and 1984.

Both years, notes Hunt, are leap years and Presidential election years. And in both years the U.S. hosted the summer Olympics. All three characteristics tend to add to growth through the end of summer: leap years by providing an extra day of income and spending, and the Olympics and political conventions by boosting outlays.

In 1984, the economy boomed in the first half and slowed significantly with the onset of fall. As a result, long-term interest rates fell sharply in the year's final four months. "If it happens again," warns Hunt, "don't be surprised."

HOW LOW SHOULD INFLATION GO?



toll on U.S. economic performance that would far outweigh its vaunted gains.

The problem is not the temporary pain of moving to zero inflation. Rather, it's the way zero inflation would affect the ability of companies to lower labor costs when their business is poor. In a free-market economy with at least a modicum of inflation, companies doing badly can reduce their relative wage bills by giving low pay hikes, or none at all, even as those doing well dole out above-average increases. Under zero inflation, however, the room for such adjustments would be severely constrained.

As a result, companies needing to reduce their relative wages could only do so either by cutting paychecks (thus hurt-

AMES C. COOPER & KATHLEEN MADIGAN

SOMETHING'S GOTTA GIVE AND IT'S LIKELY TO BE PROFITS

Unit labor costs are up, but tightfisted shoppers may keep a lid on prices

U.S. ECONOMY

It had to happen sooner or later. One of the key trends that has shaped this 5½-year expansion—compliant unit labor costs—is taking a turn for the worse: Costs are beginning to outpace inflation.

Big deal? Well, yes. Unit labor cost—the labor cost per each unit of output—is the key determinant of pricing for most businesses. If the cost of making a good or service exceeds its price, you lose money. For the past 4½ years of this business cycle, unit labor costs have lagged well behind the growth of prices. That meant companies didn't have to hike prices to make money, enjoying cushy profit margins even when pricing power was nil. Now, this linchpin of the low-inflation, low-margin economy is eroding.

UNIT LABOR COSTS OUTPACING INFLATION

UNIT LABOR COSTS



PERCENT CHANGE FROM A YEAR AGO
UNIT LABOR COSTS
INFLATION
A: LABOR DEPT., COMMERCE DEPT., BW

Unit wage pressures from a tight labor market and slowing productivity growth mean the halcyon days of the inflation outlook are over for this expansion. Unless the economy slows sharply, the growth in unit labor costs will put businesses between a rock and a hard place. Companies will either have to raise prices to watch their profit margins slip.

MOST LIKELY OUTCOME

At least in the near term, it appears to be a little bit of both, but the bigger risk is more likely to hit profits. That's because the pricing climate is still tough at a time when labor costs, which account for about three-quarters of the average business' expenses, are rising.

Unit labor costs grew at a sharp 3.8% annual rate in the second quarter. Over the past year, unit costs have risen 3.1%—far above the 2.1% advance in prices economy-wide, as measured by the gross domestic product price index (chart).

This gap started in the middle of 1995, about the time when the unemployment rate fell low enough to

generate positive real wages and after productivity growth lost its cyclical gains. Output per hour worked in the nonfarm business sector slipped 0.1% last quarter. For the year, it's up only 0.7%.

Manufacturing efficiency rose 1.5% last quarter, but that gain was well below the recent trend. And given the quarter's 5.8% surge in compensation, factory unit labor costs jumped 4.2%. Although the trend in manufacturing productivity remains impressive, some of the gains are misleading. More and more factories rely on workers supplied by temporary-help agencies. And temps are counted as service-sector payrolls.

Businesses are unlikely to get much cost relief in coming quarters. A 5.4% unemployment rate means companies are scrambling to find skilled workers. And while demand is slowing, the rise in third-quarter GDP right now seems closer to 3% than 2%. After last quarter's 4.2% gallop, that's fast enough to make labor markets even tighter and to create capacity constraints.

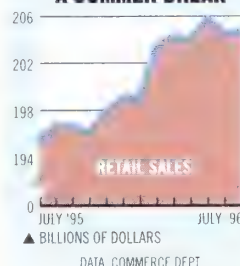
A CONSUMER SLOWDOWN

was evident at the nation's stores and shopping centers in July (chart). Retail sales edged up 0.1% last month, but that followed a revised 0.5% drop in June. Excluding autos, sales did look healthier, with a 0.3% gain erasing June's 0.2% decline. Real retail volume started the third quarter down a bit from the second-quarter level.

However, buying in early August looks better. The Mitsubishi Bank/Schroder Wertheim survey says store sales were up 0.6% from July. And the *Johnson Redbook Report* showed a stronger 1.8% gain. A solid August is vital for retailers because it includes the key back-to-school season. The upbeat August data suggests that shoppers in July were distracted by TV coverage of the Olympics and that July's unusually cool weather hampered sales of hot-weather items.

Shoppers remain cost-conscious, though, in part because they have other uses for their money, such as saving for college and retirement and paying off debts. For retailers, these discount devotees are punishing the bottom line. Even at their meager growth rate, producer prices of core consumer goods, which excludes en-

SHOPPERS TOOK A SUMMER BREAK



▲ BILLIONS OF DOLLARS

DATA: COMMERCE DEPT.

ergy and food, are rising faster than stores can mark up merchandise (chart).

Consumer discount-hunting helps to explain why the price indexes show little upturn. Consumer prices of goods and services rose a higher-than-expected 0.3% in July. The gain for core prices, which exclude food and energy, was also 0.3%. In the past year, consumer inflation is running at a mild 3%; the core rate is 2.7%.

Back at the wholesale level, the producer price index for finished goods was unchanged in July, while core prices rose just 0.1%. Over the past year, the total PPI has risen a mere 2.6%, and the core rate is only 1.5%. Further back in the production process, prices for core intermediate materials are down 1.8% from a year ago. Prices for core crude goods are down a steep 13.5%.

FOR CONSUMER INFLATION, two areas worth watching are housing and food. Housing costs have been trending higher because demand remains quite healthy. The July rise of 0.4%, though, reflected a 2.3% increase in lodging away from home. That jump is unlikely to be repeated, but rising home prices and rents will keep total service inflation from slowing further.

Food inflation is a bigger worry. In the past three months, food prices have risen at a 5.1% annual rate, the largest three-month gain in five years. Crop shortages may worsen the trend. Pointing to bad weather, the Agriculture Dept. cut its forecast for this year's corn har-

vest by 4.7%, suggesting that grain shortages will continue into 1997.

That won't mean just costlier tortillas. Corn is used for sweeteners, livestock feed, and cereal. So higher corn prices will increase the cost of many grocery items for months to come. The key question is whether consumers will accept the markups. Even as grain prices have risen, cereal makers such as General Foods and General Mills Inc. have cut prices steeply to attract more customers. The first casualty of the price war: Ralco Holdings Inc. will sell its cereal brands to General Mills.

So too, carmakers are trying to ease sticker shock (page 30). Each of the Big Three has announced that the average price hike on its 1997 vehicles will be under 2%. And Chrysler Corp. is even putting rebates on some 1997 models.

Squeezed by rising labor costs, companies hope such spare markups will soon fall by the wayside. After all, the gain in real buying power from higher wages should make consumers more willing to accept price increases. It seems a straightforward trade-off. The problem for profit-seeking companies, though, is that it's not yet certain that consumers will play along.

RETAILERS FACE RISING COSTS



CANADA

WILL RATE CUTS SPELL RELIEF?

What will it take to pull Canada out of its malaise of high unemployment and weak consumer demand? The Bank of Canada may have the answer.

The BOC cut interest rates by a quarter-point on Aug. 9 for the second time in three weeks. The cuts since May, 1995, now total 3½ percentage points. And with the target range on banks' overnight lending rate now down to 4% to 4½%, Canadian monetary policy is the most accommodative on record. Moreover, with inflation possibly set to slip below the BOC's 1%-to-3% target and with the Canadian dollar stable, further rate-cutting cannot be ruled out.

Weak job data for July con-

firmed that the economic bounce after the November vote on Quebec sovereignty has petered out. Retail sales have been flat since January. And after inflation dipped unexpectedly, to 1.4% in June, the BOC felt a move was justified. The financial markets agreed.

Canada is really two economies right now: one fueled by net exports, primarily auto shipments to the U.S., and one beset by slumping domestic demand, mainly weak

consumer spending. Consumers are constrained by soft job markets and public-spending cuts.

Quebec is responsible for some of Canada's split personality. The province accounts for 23% of the

country's jobs, but since February, Quebec payrolls are down 90,000 (chart), while jobs elsewhere in Canada are up 73,000.

Strong exports and flagging imports propelled the trade balance into a record surplus last quarter, fueling manufacturing output. Trade improvement appears to have added some two percentage points to second-quarter economic growth, expected to be in the 2%-to-2½% range. Trade is also a key support under the Canadian dollar, along with low inflation and progress toward better control of government finances. Lower interest rates are already lifting housing. Businesses have revised up their capital-spending plans. And the huge rate cut will ultimately spur a resurgence in consumer spending, all to the benefit of second-half growth.

QUEBEC SKEWS CANADA'S JOB NUMBERS





gives Sega the winners.



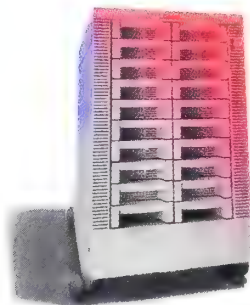
Virtua Fighter 3

Honeywell the control.



TotalPlant Solution System

Data General the command.



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MOTOROLA

What you never thought possible.

THE REPUBLICANS

DOES HE HAVE A CHANCE?

Dole's tax plan, Kemp, and the show in San Diego may avert disaster, but...

As televised productions go, the Aug. 12-15 Republican convention in San Diego set new standards for political theater. Their spirits lifted by GOP nominee Bob Dole's embrace of both Reaganesque tax cuts and supply-side hero Jack F. Kemp, convention-goers departed San Diego convinced that the long-shot campaign was maybe, just maybe, winnable.

More important for the Dole-Kemp ticket, a carefully scripted convention tableau left millions of television viewers with the image of a party committed to tolerance and inclusion. Although right-wingers made up the bulk of the delegates, once the cameras rolled, they were rarely seen. Crows freshman Representative Zach Wamp (R-Tenn.): "We kept divisive social issues out of the hall." By spotlighting women and minorities, from keynote speaker Representative Susan Molinari (R-N.Y.) to New Jersey Governor Christine Todd Whitman to retired General Colin L. Powell, Dole strategists beamed a powerful message to voters: Dole can be trusted to champion compassion—as in nonscary—conservatism.

Dole repeatedly drove the point home in remarks prepared for his Aug. 15 acceptance speech: "The fundamental issue is...trust—not merely whether the people trust the President, but whether the President and his party trust the people." Unfortunately for Dole, he's not angling for an Emmy Award for Best Political Choreography. He's after the Presidency. And Dole's strategists concede that he still faces a steep uphill climb. Admits a senior aide:

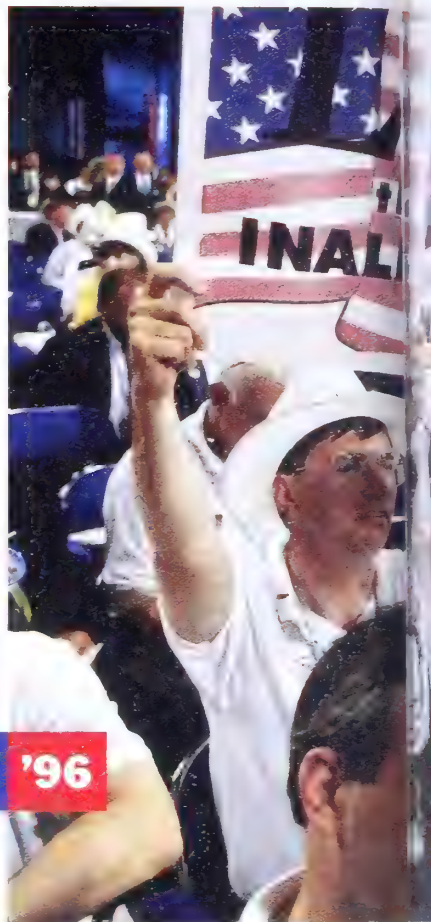
"We have precious little margin of error."

Here's why: Despite the convention love-fest, Republicans are less united than they appear. Hardliners don't consider Dole a True Believer and mutter that his supply-side conversion is mere expediency. "Republicans are not Marxists who vote for anyone who says 'tax cuts,'" sniffs conservative activist Paul Weyrich. "It'll take more than tax cuts to elect Dole, because many people think he's a Washington hack."

Social conservatives, for their part, sense that Dole is uncomfortable with their issues, from strict abortion curbs to calls for *kulturkampf*. Even the selection of Kemp causes concern. Kemp's desire to reach out to minorities and oppose curbs on immigration and affirmative-action programs is at odds with their plans to create new "wedge" issues to use against Democrats. "We have a fractured conservative movement," says Texas GOP Chairman Tom Pauken, whose delegation was nearly torn apart by the Christian Right's drive to purge pro-choice Dole supporters. "The splits are getting more difficult to reconcile."

CLINTON CENTRISM. Despite their qualms, conservatives will vote overwhelmingly for Dole come Nov. 5. Their hatred for President Clinton guarantees that. Dole's larger problem is stubborn resistance from women, moderates, and suburban independents. Lured by the President's new centrism, up to 20% of GOP voters have drifted into the Clinton column. Meanwhile, the solid economy and a Presidential values barrage have kept

ELECTION '96



defections of blue-collar Reagan Democrats to a minimum.

At the moment, Clinton has a commanding lead with suburban swing voters. Many are put off by Dole's ties to the gun lobby, Big Tobacco, and anti-abortion forces. "It's death for Dole to be so weak in the suburbs," says Terry Madonna, a political scientist at Millersville University in Pennsylvania. Dole aides, however, believe his new emphasis on economic incentives will be boffo in the 'burbs. "Suburban voters tend to be extraordinarily tax-sensitive," says Dole pollster Anthony Fabrizio. "That's going to help us in places like

THE TICKET'S BIG CHALLENGES



IT'S THE ECONOMY, BOB

Dole has to keep the debate focused on his plan for a 15% across-the-board tax cut as a way to boost growth and wages. The problem: The Clinton economy is humming at



Jersey, Connecticut, and Illinois." Despite Dole's attempt to turn the election into a political *Oprah* show, problems with women voters continue. Unless he can narrow the 20-point gender gap, there's no way he can win. Says New Jersey's Whitman: "We still need to convince [women] that this is not a party of intolerance." Beyond Dole's woes with specific voters, the overall challenge of regaining votes away from Clinton amid economic expansion. Dole's answer to voter anxiety is an income-boosting tax plan built around a 15% across-the-board tax cut and a \$500-per-child tax

credit. But on the stump, voters go blank when he talks about "the Clinton Crunch." White House aides sneer that the Dole economic plan is so business-friendly—and its benefits so tilted toward the rich—that it lacks credibility as a way to ease middle-class economic angst.

Elitist nonsense, reply the Dole folk. Says Communications Director John Buckley: "Look, this election has just begun anew. Dole has transformed an issueless race in which Clinton passed himself off as a moderate into a debate about the economy." Adds Vin Weber, a senior campaign issues adviser: "This

SOUND AND FURY Big-tent talk and slick TV can't hide the reality that the Grand Old Party is still a house divided

is a debate we're going to win."

That may be, but Dole has very little time to get his campaign in fighting trim. Although he wrapped up the nomination in the spring, Dole failed to consolidate his party base until the convention—months behind schedule. "The economic trends are against us. The calendar is against us," says one Dole adviser. "But if Dole can convey a new compassionate image for the Republicans, we have a chance."

NARROW WINDOW. There's no question that Dole's "kinder, gentler" convention helped his cause. Now, he needs to keep the momentum going. In coming weeks, Dole and Kemp will relentlessly pound home the ticket's promise of big tax cuts while reminding voters of Clinton's tax flip-flops. And Dole will harp on Americans' gnawing unease about crime, drugs, and social decay. For instance, Dole is weighing a new anti-crime package that requires juvenile offenders to work or take mandatory courses. Says an aide: "It's a two-part strategy, stressing economic and personal security. We've got to drive Clinton to the left on taxes and moral issues."

Dole has an opportunity to make the election a real contest. But only if he focuses on his tax-cut message—and his battle plan unfolds with a precision that has not been a hallmark of his campaigns to date. The window of opportunity, moreover, is narrow, and Dole's ability to keep his composure in the difficult days ahead is an unknown. One special nightmare haunting his handlers: looming debates in which he could be overshadowed by Clinton's glibness and Ross Perot's tele-zaniness.

Ultimately, a sizzling Veep and a well-orchestrated convention show can only take Dole so far. To go the distance, he'll have to persuade skeptical Americans to trade one unloved career politician for another in November.

By Lee Walczak and Richard S. Dunham, with Mary Beth Regan in San Diego

Will Kemp's tax-cut promise win him votes? But it may not be enough. Sniffs conservative pundit H.W. Harkins: "Republicans are not Marxists who vote for anyone who says 'tax cuts'."

CREDIBILITY

Dole's economists at the spend-Dole has so far don't tax breaks. e to lay out to be credible, will give the ts more ammo.

BROADEN THE BASE

Reaching suburban independent swing voters and narrowing the gender gap are crucial. Many of these voters are turned off by links to the Christian Right and skeptical of Dole's Reaganesque tax plan.

SHORE UP SUPPORT

Dole must strengthen his base in such traditional GOP states as Florida and Arizona. But key voter blocks are resisting his message, among them seniors, Catholics, and women.

PICK UP THE PACE

In San Diego, Dole consolidated his conservative base and began bringing Republicans home. However, he may not have enough time to instill a positive image of himself with voters.

THE CANDIDATES

HOW TO LOSE FRIENDS AND INFLUENCE ELECTIONS

Perot's star has fallen, but three-party politics is on the rise

Ross Perot is plagued by high negative ratings, sagging voter support, and splits within his own infant third-party movement. But that isn't deterring him from elbowing his way into the 1996 campaign.

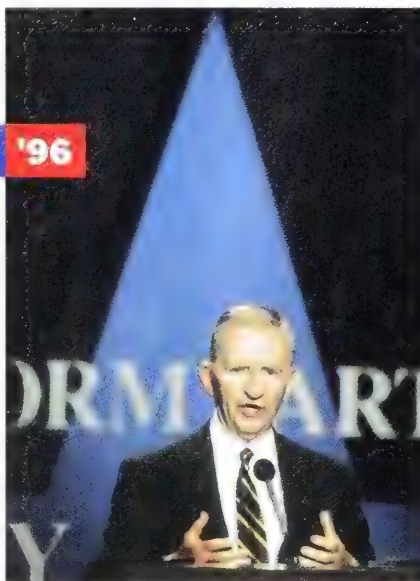
The unpredictable billionaire may be little more than a nuisance for Bill Clinton and Bob Dole, but he's a nuisance who could influence the outcome of both the Presidential and congressional elections.

That's why Republican and Democratic strategists were watching warily as Perot's Reform Party geared up to announce its first Presidential ticket on Aug. 18 in Valley Forge, Pa. Former Colorado Governor Richard D. Lamm gamely tried to win the party's nomination, but Perot was the overwhelming choice of delegates at the Aug. 11 party convention in Long Beach, Calif.

Assuming he wins the Reform Party nod, few analysts expect the feisty Texan to approach the 19% vote he received in 1992. He would garner 12% in a three-way race with Clinton and Dole, according to a Gallup Poll of 1,003 registered voters conducted Aug. 5 to 7.

"ROMAN CANDLE." More ominous for Perot, he has been unable to recover from a slide in public approval that followed his November 1993 free-trade debate with Vice-President Al Gore. With Perot's public persona transformed from crusading reformer to quirky publicity hound, his negatives have shot up to 53%, according to Gallup. Little wonder political pros are writing him off as a serious contender: "He's like a Roman

ELECTION '96



CATALYST: Perot could force Clinton and Dole to deal with thorny issues

candle," says GOP Texas Governor George W. Bush. "He shines brightly for a while. But four years later, his spark diminishes."

Perot is facing defections even within his own Reform Party. Polls show that nearly half of Perot's '92 supporters will abandon him this year. Says Heidi Fineberg, a Lamm fan from Reseda, Calif.: "We couldn't have had a party without him. But we've grown beyond him."

Still, even a diminished Perot can alter the dynamics of the campaign. He'll use his wealth and a spot in the Presidential debates to gain airtime to frame

the issues, forcing Clinton and Dole deal with controversial subjects such as entitlements and campaign-finance reform. "He will shape the tone of the campaign," predicts independent pollster Gordon S. Black.

Republicans worry that, in the event the third-party contender will attract anti-incumbent voters who otherwise would have gone to Dole. "A vote for Perot is a vote for Clinton," says GOP Chairman Haley Barbour. Democratic strategists initially agreed with Barbour's view. But now, they fret that the Texas maverick could siphon off critical blue-collar votes from the President's key swing states such as Michigan, Illinois, and New Jersey. Polls are no help. They show Perot drawing evenly from the President and the GOP nominee.

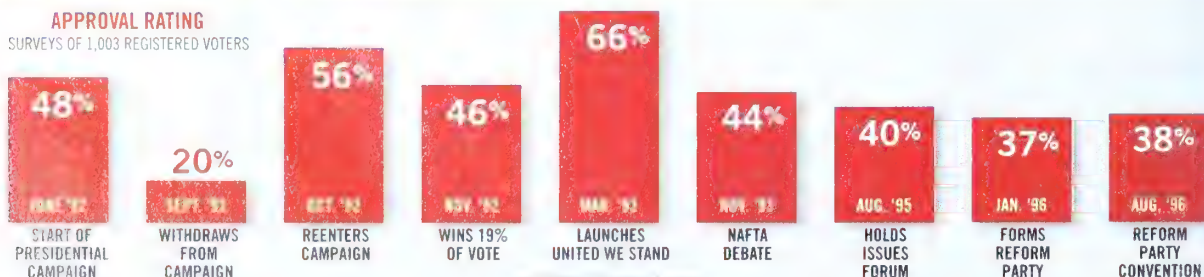
Beyond the Presidential race, Perot followers could determine which party wins control of Congress. In 1994, two-thirds of the Perotistas voted Republican, helping to end the Democrats' reign on Capitol Hill. This year, the Reform Party hopes to flex its muscle by endorsing candidates in every congressional race. And the impact is unclear. The GOP could benefit because its candidates support such Perot staples as a balanced-budget amendment and term limits. But Democrats could win Perotista votes by stressing fiscal restraints and campaign-finance reform.

On the face of it, Perot probably will not succeed this year. "If you look at the whole history of third parties, no candidate has run twice in a row and gotten 5% of the vote," says American University historian Allan J. Lichtman. Still, while Perot himself may be a fading presence, the third-party movement he inspired remains a force to be reckoned with. Chances are, it will play a crucial role in determining which major-party politicians will lead the country—and where they will take it.

By Richard S. Dunham in Long Beach, Calif.

PEROT'S UPS AND DOWNS

The fluctuations in Perot's popularity have made it hard for the major parties to predict how many voters will defect—or even to which side



By Howard Gleckman

DOLE'S RELUCTANT RANK AND FILE

f the ideological conservatives who increasingly control the Republican Party at the grassroots had their way, Bob Dole's mellow '96 convention would have had a starkly different look. On the podium would have been a succession of hardline heroes: televangelist Pat Robertson, abortion foe Phyllis Schlafly, and populist crusader Pat Buchanan. Their topics: abortion, school prayer, and immigration reforms—hardly the issues the GOP nominee wants to run on.

Increasingly, Dole and running mate Jack Kemp are leaders without followers in their own party. Today now, 15 to 20 state parties are controlled by the Religious Right. And their Republicanism is a far cry from the mainstream Big Business philosophy that spawned Dole—and from the pro-growth neoconservatism embodied by Kemp. "Dole has tried to manage a moderate message in a house full of conservatives," says Carleton College political scientist Steven E. Schier.

The party nominees support free trade and federal protections of civil rights, while much of the New Republican rank and file does not. Dole and Kemp give lip service to federal restrictions on abortion. For the Religious Right, an absolute federal ban is the highest priority. It's the pro-life advocates who are the foot soldiers of this movement," says Calvin Ebner, a county GOP chair from Deweyville, Tex. "I think we're the future of the party."

UNCOMFORTABLE CEOs. Even when Dole and Kemp are in sync with the social conservatives on issues such as tax cuts, their goals and motives diverge. Dole and Kemp see the tax code primarily as an instrument to provide economic incentives, so their focus is on across-the-board rate cuts and reductions in capital-gains taxes. By contrast, the Religious Right regards the tax code as a means to influence social behavior. Their priority

is tax breaks for adoption, families with children, and charitable giving.

While Dole and Kemp are both solid free-traders, many of the GOP delegates are economic nationalists in the populist image of Pat Buchanan. "It's not a radical trade policy. It's common sense," says Drew R. Ivers, Buchanan's Iowa state chairman. "Dole and Kemp will have to move

But tolerance doesn't sell with the New Republicans. TV viewers watching retired General Colin L. Powell heard only scattered boos when he told the convention that he supported abortion rights and affirmative action. What they didn't see were the hundreds of stone-faced delegates sitting on their hands as he preached his message of inclusion. And the

party platform is absolute in its opposition to affirmative action, immigration, and abortion. Dole might downplay the document, but he will come under intense pressure, if elected, to adhere to it. Already, on Aug. 12, Kemp tried to appease the Right by backing away from his longstanding opposition to a California ballot initiative to repeal affirmative-action programs.

The attitude of many ultraconservatives toward Dole has been extraordinary: They are supremely indifferent to the results of the coming election. Instead, they're focused on state and local challenges and the Presidential race in 2000 and beyond. One indication of how completely the Religious Right dom-

inates the GOP: Just days before the convention opened, aggressive anti-abortion candidates whipped mainstream rivals for GOP Senate nominations in Georgia, Michigan, and Dole's own Kansas.

These deeply committed, hard-working apparatchiks came to San Diego to consolidate control of their party. The real story of this convention is how far they've advanced. For now, they're stuck with Bob Dole and Jack Kemp, candidates they don't completely trust. But as they look to the next millennium, they are bent on remaking a Republican Party in their image. A party that Bob Dole, Jack Kemp, and Corporate America won't recognize as their own.

Gleckman covered his first convention in 1972.



ROBERTSON AND FAN The real story of San Diego is the Right's tightened grip on the GOP. For now, it's stuck with two candidates it doesn't trust

toward that position." Similarly, the New Republicans favor strict curbs on immigration. That view contrasts sharply with the interests of many businesses—especially high tech—that rely on immigrant workers.

But the biggest difference between the GOP's Presidential ticket and party activists is on social issues. While both Dole and Kemp are anti-abortion, both candidates have long records as social moderates on other issues. Dole, for instance, is very proud of his support for civil-rights legislation of the '60s and his authorship of the Americans With Disabilities Act. Kemp has always seen himself as a spokesman for racial tolerance and social inclusion. That attitude plays well in Corporate America's boardrooms, where CEOs are uncomfortable with the Religious Right's agenda.

EXECUTIVE SUITE

SLASHER AT LARGE AT SONY PICTURES

Still recovering from the Guber era, it faces new bloodletting

For Alan J. Levine, president of Sony Pictures Entertainment, a trip to Hawaii quickly turned into a lousy summer vacation. Early August news accounts from the mainland had him being forced from his job as Sony's top Hollywood executive, and the fax machine in his room at Maui's Four Seasons Hotel was spewing out urgent messages. Finally, at 11 p.m. Maui time on Aug. 7, he reached Sony Corp. President Nobuyuki Idei in Tokyo, who he says assured him that his job was secure.

For Sony's Hollywood execs, job security is always a topic of high drama. Since 1989, when the Japanese electronics giant paid \$3.4 billion for Columbia Pictures, an amazing number of moguls have departed. In all, Sony's top U.S. executive, two entertainment unit chiefs, and four studio chiefs have taken mega-buck severance packages. Now, it seems, the turnstile may spin again.

DOG DAYS. Wracked by a horrid summer at its film unit, Sony's Tri-Star Pictures Inc. head Marc Platt, Columbia Pictures President Lisa Henson, and top marketing executive Sid Ganis have all left since mid-July. And now Levine is carefully reviewing all deals done by Mark Canton, who runs Sony's combined film operations for Levine. Canton will be sent packing if the schedule contains any hint of money-losing films such as this summer's *Multiplicity* and *Sunset Park*. Further up the chain of command, Jeff Sagansky, overall strategic planner for Sony's film and music units and Sony's top American in the U.S., is said to be mulling a departure from his job. Sagansky declined to be interviewed.

As for Levine, a 49-year-old onetime entertainment attorney, things look secure for now. One of the few holdovers from the spendthrift five-year reign of

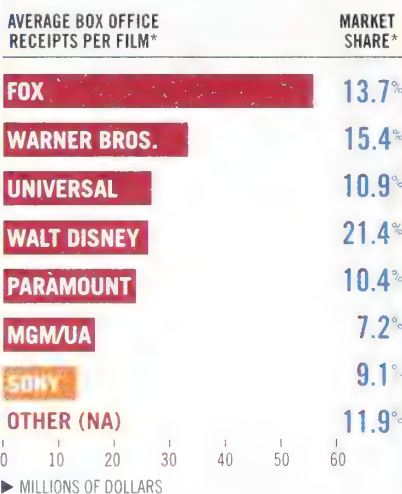
former Sony studio chief Peter Guber, Levine has won high marks for cost-cutting. His pruning has helped give Sony six consecutive profitable quarters after taking \$3.2 billion in write-offs in 1994. A strong TV unit and a new German TV deal lifted revenues in the quarter ended June 30 by 84%, to \$977.3 million. "Just look at the numbers," says Levine. "We've been doing the job that has been asked of us."

But how long Levine's job will stay



IDEI: The No. 1 mission is to keep costs down

BACK OF THE PACK



LEVINE: Despite rumors, his job looks secure

secure is unclear. The final say rests with Idei, who one former Sony executive says "will make his own decision in his own time." Sony issued a tepid show of support for him in a letter to studio executives from Sony Deputy President Tadasu Kawai. In Levine's favor, Columbia's TV operations still do well. But its film unit has faltered lately. The Jim Carrey comedy *The Cable Guy* has grossed just \$58 million, far less than Sony anticipated. And the upcoming *Devil's Own* was plagued by personality clashes between actors Brad Pitt and Harrison Ford—and zoomed nearly \$20 million over its \$67 million budget.

Insiders say Sagansky, who was passed over for the top U.S. job when Sony Corp. of America Chairman

Michael P. Schulhof quit under pressure in late 1995, has openly promoted longtime friend and former Home Box Office Inc. Chairman Michael J. Fuchs for several jobs at Sony. Among them: Levine and that of music-unit chief Thomas I. Mottola. Fuchs flatly denies he has sought any Sony job.

Meanwhile, Idei authorized Levine to fashion a relatively puny studio spending strategy. Sony is spending \$100 million annually and has launched, mostly in partnership with others, 13 cable channels in such places as Asia, Latin America, and India to air some of its 3,400 films and 35,000 TV episodes. Since 1994, it also has operated the Game Show Network, which airs episodes from its 61 game shows, which include *Family Feud* and *Wheel of Fortune*.

Otherwise, Sony is moving slowly in the U.S. Foreign companies are pro-

hibited from buying U.S. TV networks outright, but CBS Inc. looks to be a possible partner. Michael H. Jordan, CEO of Westinghouse Electric Corp., which bought CBS last year, met with Idei in mid-July to discuss potential ventures. "We've talked on an ongoing basis with Sony," says a senior CBS executive who says possible deals could arise in cable TV, expanded programming alliances, or an international joint venture.

Meanwhile, Sony's studio needs some winners. Insiders predict good things for such new attractions as *The Fan* with Robert De Niro and *Jerry Maguire*, a Tom Cruise vehicle. The question is which Sony executives will be around to check the box office.

By Ronald Grover in Los Angeles
with Elizabeth Lesly in New York



TELEVISION

TIME TO SAY GOODNIGHT, DAN?

CBS Evening News slides, the anchor's seat gets hotter

Dan Rather is still big. It's the audience that got small. Take the viewership of Rather's *CBS Evening News* in Albany, N. Y. At 6:30 p.m., 27% of all televisions in that market are tuned to the local news show of WRGB, the CBS affiliate, outperforming the national news shows of ABC and NBC. Come 7 p.m., it's

Rather time, and nearly half of CBS's viewers flee. The Rather show has lost the momentum of its healthy lead-in and pulls only a 16% share.

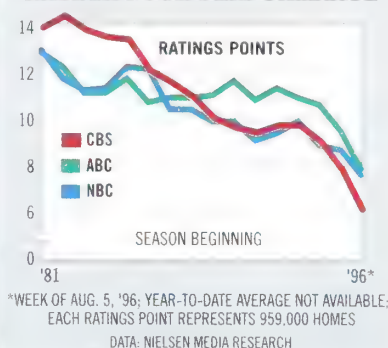
Nationally, the ratings performance of *Evening News* has never been worse. When Rather inherited the anchor's chair from Walter Cronkite in 1982, he also inherited a 14.4 rating and a 25% share. Though the ratings of all three network news broadcasts have shrunk as cable viewers have jumped to cable, CBS's decline has been the most dramatic (see chart). For the first prime-time broadcast of the Republican convention, CBS lagged behind ABC and NBC. For the week of Aug. 5, Nielsen Media Research says Rather's broadcast scored a national rating of only 2.6, a little better than its 5.4 performance the week of July 1, a historic low for a network news show, Nielsen says. In Los Angeles, *CBS Evening News* earns a rating of just 2.6, and in New York 3.0—less than half the score of the ABC and NBC news shows in each city.

That's a major problem for CBS and

Westinghouse Electric Corp., which bought the network last year. Network news is a key opportunity to line up viewers for an evening's prime-time fare, as well as being a cornerstone of a network's prestige. And the continuing weakness at *CBS Evening News* has affiliates grouching. "The problems of CBS News are much, much more intractable" than at other CBS divisions, says Alan Bell, president of the broadcast division of WRGB parent Freedom Communications Inc.

Part of the problem may be Rather himself. "Rather is a person with no middle," says Bell. "He has passionate loyalists and passionate detractors." Eric Braun, a consultant with Frank N. Magid

RATHER POOR PERFORMANCE



ASSIGNMENT, HAITI

"Dan has never looked better," says CBS News chief Heyward. But "over time we can't just sit there and do nothing"

Associates Inc., also argues that CBS has miscalculated by continuing to make the program "star-centered" while years of cost-cutting have depleted the ranks of second-tier stars who might have added to its allure. "The product is out of whack," says Braun, who thinks many of those

who still tune in do so out of habit.

The question now is what, if anything, CBS or Westinghouse will do to halt the slide. In just seven months on the job, CBS News President Andrew Heyward already has rejiggered *60 Minutes* and *48 Hours* and has completely reconfigured CBS's morning news show. But Heyward seems wary of changing *CBS Evening News* drastically. "We're not panicking. The program itself is very strong and getting stronger. Dan has never looked better," he says. But the ratings deterioration, Heyward admits, "is a matter of frustration. I'd like to see us competing more effectively. And over time, we can't just sit there and do nothing."

"NOT SHOPPING." Short of replacing Rather, which senior CBS executives say is not under consideration, what can be done? Heyward says if the ratings don't improve on the strength of the broadcasts alone, he may fiddle with the show's promotion and format. And he's talking to major news stars at other networks as their contracts expire. Heyward won't confirm talks with any individuals. But there are plenty of prospects who are free to strike a deal in the coming year, including Diane Sawyer and Ted Koppel at ABC and Bryant Gumbel and Tom Brokaw at NBC. "We're not shopping around for someone to plug in [Rather's place] right now," says Heyward, but "Dan is fully aware of the need to bring people into CBS news. We're looking at news superstars for a person who could step into that role eventually."

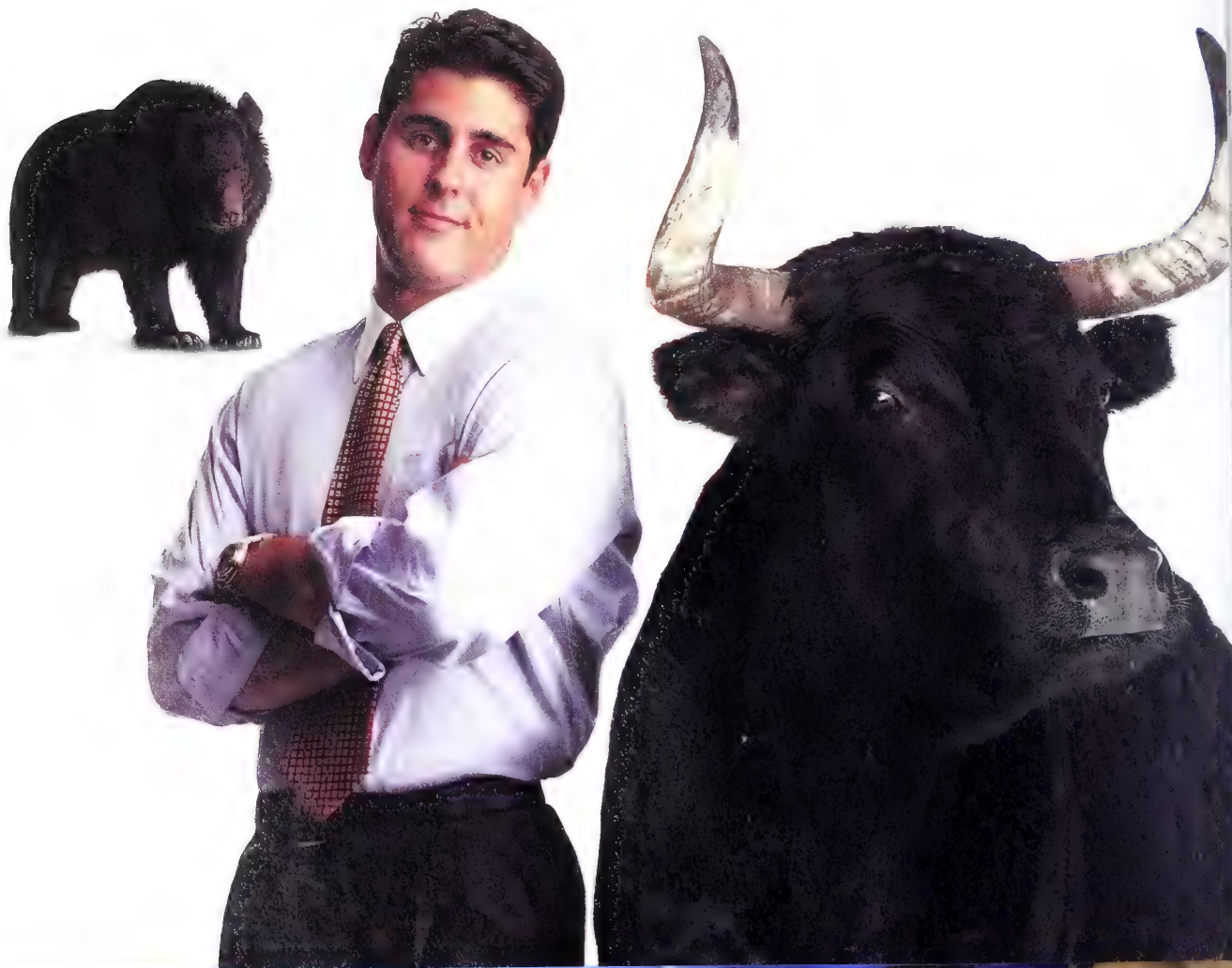
Rather may well stay put until his current contract (salary: an estimated \$5 million annually) runs out at the end of 1999. But some affiliates don't want to wait that long. "Dan has gone downhill ever since that [contentious 1988] interview with George Bush. The show has lagged in the ratings for a long time. Steps have to be taken," says Gray Communications Systems President Ralph Gabbard, who heads the CBS affiliates' board. Being a distant third in network news "means [losing] money, prestige, and pride," he says. That's a situation the network may not be able to tolerate all that much longer.

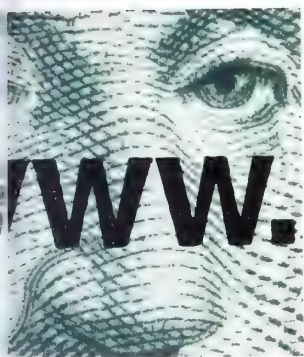
By Elizabeth Lesly in New York

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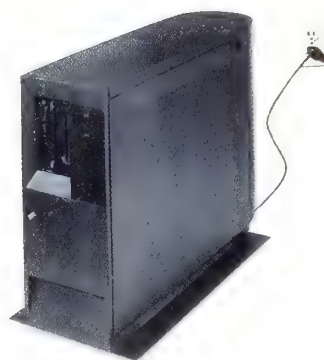
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AUTOS

SMOKE AND MIRRORS
IN DETROIT

Why Big Three price hikes only look modest

In Detroit, it's the year of the stealth price increase. The Big Three auto makers proudly announced 1997 model prices in recent weeks, bragging that they subdued sticker shock by restricting increases to less than 2%. But what the companies didn't crow about were the hikes on many models that they quietly instituted in the preceding months. "You can't hoodwink people like this," grouses suburban Detroit auto dealer Martin "Hoot" McInerney.

Maybe not, but the Big Three clearly have decided it's time to take profits on their hot-selling trucks. Ford Motor Co., for example, double-dipped on price hikes for its popular F-150 pickup truck and Explorer sport-utility vehicle by raising stickers quietly on July 1 and then publicly announcing another boost on Aug. 8. General Motors Corp. stealthily raised prices on its sport-utility vehicles and small pickups back in April, then boosted them again on June 27. Chrysler Corp. triple-dipped on its star minivan, hiking its price in January, March, and July. It also slipped in an



GRAND PRIX: Restyled and repriced—upwards 5.4%

unannounced increase of \$472 to \$500 on its popular Jeep Wrangler on July 12—just days before announcing official fall hikes averaging 1.9%, or \$422.

BACKLASH? Detroit could be in for a rude awakening when Japanese rivals announce prices in the coming weeks. The softening yen gives the Japanese leeway to lower prices by up to \$800 per car, figures Morgan Stanley & Co. analyst Stephen J. Girsky. Just as bad for Detroit, notes independent auto consultant Christopher W. Cedergren, "this strategy may slap [Detroit] right back in the face by causing a slowdown in the whole light-truck market."

Ford's recent pricing decisions show

THE BIG THREE'S L

FORD says its 1.2% (\$281 per vehicle) price increase for 1997 is the smallest among the Big Three. But on July 1, it quietly raised prices on its hot-selling Ford Explorer and pickups.

▼ **GENERAL MOTORS** hiked prices on its 1997 models by an average of only 1.7%, or \$391, but that's on top of the hikes the company eased through in April. GM hasn't set prices for most of fall's many new models.

just how crafty Detroit is getting. The company boosted Explorer prices by \$200 on July 1 and then piled on additional hikes of \$315 to \$685 to the model's price in its official Aug. 8 pricing announcement. Ford says its 1997 model prices were up an average of only 1.2%, or \$281—the lowest among the Big Three. But its computations don't include the July 1 price hikes on the Explorer and F-150, which account for a quarter of its U.S. sales.

GM also played hide-the-hikes. In announcing boosts of 1.7%, or \$391 per vehicle, it omitted prices on a huge crop of overhauled models coming this fall. A GM spokesman says it is unfair to compare prices on redesigned models, which are packed with new features, with those of previous models. But dealers say many shoppers don't buy that logic.

THE BIG THREE
TO THE UAW:
PICK ME! PICK ME!

It's a three-way race, and only Stephen P. Yokich knows the winner. On Aug. 22, the United Auto Workers president will announce which Big Three auto maker gets first crack at negotiating a new labor accord. Chrysler Corp. remains the likeliest choice, but Ford Motor Co. and General Motors Corp. are still making plays to be chosen. The reason: The first one to bargain gets to set the industrywide pattern for wages, benefits, and job security—or face a strike.

When contract talks opened in June, Chrysler's huge profits made it seem

the most likely to agree to job preservation and big wages hikes. But, says Chrysler President Robert A. Lutz: "It's less and less a foregone conclusion that we are the target." Chrysler has made it clear it won't give up the flexibility of buying more parts from outside suppliers—though the UAW still thinks it may bend at a strike threat. "The profits are so enormous, I don't think Chrysler would want to shut down for even a day," says a union source.

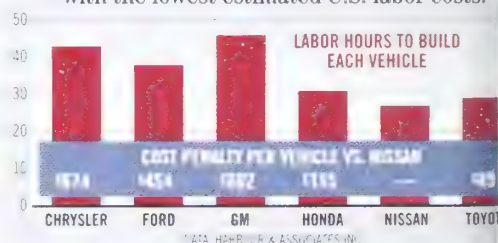
OLIVE BRANCH. Meanwhile, Ford and GM have been jockeying for UAW attention. Yokich calls the UAW's relationship with Ford "very good." Adds Edward E. Hagenlocker, president of Ford's auto operations: "We have a

proven track record of being able to deal with difficult issues and reach workable solutions." Ford tossed UAW an olive branch by backing the union's drive to organize two plants run by its main seat supplier, John Controls Inc.

GM fears being the odd company. Last spring, it endured a bitter 17-

WHY DETROIT MUST HOLD THE LINE

How rivals stack up against Nissan, the auto maker with the lowest estimated U.S. labor costs:



DET: STEALTH PRICING

SLER says it raised 1997 model by 1.9%, or \$422 per vehicle. at's on top of hikes of \$95 to on the Neon and midsize cars in In early July, it slipped in hikes of to \$500 on the Jeep Wrangler.

THESE COMPANIES haven't nced 1997 model prices, but ana- ay the weaker yen may allow them e by up to \$800 on some models. e, Nissan slashed some Infiniti s 10.5%.

DATA COMPANY REPORTS, BUSINESS WEEK

For harder-to-move cars, rebates remain the rage. Ford raised the price of the most popular model in its redesigned Taurus line by \$395 for 1997, 2%. Still, Robert L. Rewey, Ford's group marketing vice-president, hints at it will keep rebates on the Taurus, which currently comes with a \$1,000 cash-back deal. "Betting that we would go to zero on incentives in the '97 model year is not a good bet," he says. Chrysler, too, is slapping rebates of up to \$1,500 on some 1997 models that aren't out yet. "Why should we lose the momentum?" asks Chrysler President Robert A. Lutz.

The bottom line, however, is going a lot more than Detroit wants to admit. The question: Will that put a damper on the new model year before it even starts?

By Keith Naughton in Detroit

by the UAW at two brake plants in , Ohio, partly because it badly o cut workers to close its produc- ap (chart). But lately it has been ig its labor stance. GM recently and plans to keep its Wilmington plant open to build a new Saturn And it cut a creative deal with ed electrical workers in Moraine, at guarantees minimum employ- ees in exchange for lower wages 7 hires. GM Chairman and CEO Smith Jr. also has been working to dispel the "labor hawk" image GM m the Dayton strike. "You always he says. "I think we settled some for the future that are important." Yokich? He says only that the will be "whoever positions them- for a settlement." Gentlemen, start igines.

Bill Vlasic, with Keith Naughton thleen Kerwin, in Detroit

DELTA EXPRESS OR 'DELTA DISTRESS'?

If its new shuttle service succeeds, it will be an industry first

The airline industry has its own version of the Edsel, and it's called Continental Lite. After less than two years of operation and more than \$100 million in losses, Continental Airlines in early 1995 grounded its shuttle operation as a hopeless exercise that confused customers, cannibalized its full-fare operations, and distressed employees.

That's why, as Delta Airlines Inc. prepares its own shuttle, Delta Express, for an Oct. 1 launch, industry wags already have christened the enterprise "Delta Distress." Rivals and industry experts alike say the plan to launch a low-cost shuttle could tarnish the airline's image, even as it fails to deliver on hoped-for savings and profitability targets. "A separate entity with a separate brand name confuses the public and takes management attention away from the main product," complains Michael Boyd, president of consulting firm Aviation Systems Research Corp.

Delta is determined to make its shuttle work. W.E. "Skip" Barnette, managing director of Delta's low-fare initiative, says Delta can run at a low enough cost with enough daily flights to make its shuttle profitable from day one.

ONLY PEANUTS. On paper, at least, Delta's plan appears to have promise. First, pilots flying the Boeing 737 planes for Express agreed in April to a 32% pay cut in a deal to return 532 furloughed Delta pilots to work. The planes will fly an average of 12 hours a day, up from Delta's average of 7.4 hours for 737s. And with first-class sections removed, Delta will be able to board more customers, who will pay only about a third of what they would pay for a same-day, one-way coach fare on a regular Delta flight.

The airline is turning its regular operations inside out in its bid to save time and money. For example, even

though the right-side engine runs air-conditioning systems, Delta Express planes will taxi into gates using only the left engine, so bags can be unloaded immediately from the cargo doors on the right side. To encourage customers to arrive early, Delta Express agents will assign seats only after passengers appear at the gate. Magazines and blankets will be stowed in back of the

planes so customers don't dawdle.

SACRIFICE. Still, along with the savings and efficiencies, Delta has built in serious potential for trouble. For example, to limit the customer confusion that was Continental Lite's biggest problem, the airline is eliminating full-fare flights on all Express routes. But that means it is sacrificing several that are lucrative. Boston-Orlando, for one, now runs 80% full. And Delta Express managers can expect morale problems as

pilots who took the 32% pay cut work alongside other employees still drawing full pay. "Delta Express may work on paper, but it's going to be difficult to work out operationally," warns David Stamey, vice-president of aviation consulting at Avitas Inc.

Then there's the Southwest Airlines Co. factor. The Dallas-based low-cost carrier will compete directly with Delta Express on at least five routes linking Orlando to Northeastern and Midwestern cities. Southwest still operates more cheaply and would have an edge in any fare war. And Southwest already is roughing up one megacARRIER offshoot, forcing United Air Lines Inc. to withdraw its Shuttle by United from four West Coast routes where it competed with Southwest. "While the war is going on, it's going to cost us very, very little," vows Pete McGlade, Southwest's vice-president of schedule planning. But it could cost Delta plenty.

By David Greising in Atlanta, with Wendy Zellner in Dallas

BUDGET ACES Shuttle pilots have agreed to take a 32% pay cut





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BOARDROOMS

AND YOU THOUGHT CEOs WERE OVERPAID

Outside directors are catching up fast

In the good old days, when shareholders rarely raised their voices, company directors would often find a crisp \$100 bill tucked beneath the dinner plates in the corporate dining room. That's when the honoraria for serving on corporate boards were sparse and the perks few.

Now, as more companies heap stock-option packages onto directors, director pay is soaring to record levels. And a new analysis of pay to outside directors by executive-compensation critic Graef S. Crystal finds many companies are grossly overpaying their overseers.

Which has the dubious distinction of having the most overpaid directors in the U.S.? Dallas Semiconductor Corp. wins hands down. Thanks mainly to stock-option grants, the custom chip-maker's outside directors averaged annual pay of \$195,200 from 1993 to 1995. Such compensation for a boardroom job, says Crystal, is 559% higher than it should be when taking into account Dallas's size and stock-market performance. **"INCESTUOUS."** Not surprisingly, perhaps, if the CEO is deemed to be overpaid, the directors who decide what the boss gets are often mightily compensated to sit in the boardroom. "There is something incestuous going on here," says Crystal. "Is it any wonder that when a CEO is paid above competitive levels, he tends to return the favor to the people who helped him out?"

Dallas Semiconductor is a case in point, according to Crystal. Besides the overpayment to the board, CEO C. Vin Prothro, who earned an average \$3.3 million in each of the past three years, or over \$9.8 million total, was overpaid by 224%, according to Crystal. Prothro says it is unfair to place a value on his or the board's option grants before they are exercised. "Valuing options like that would be like going to a fortune teller to fill out your tax return," he retorts. "If I really believed what he says, I would have to call the FBI and report a theft, because I certainly don't see \$9 million in my bank account."

The study examined director pay at 963 of the nation's largest public

corporations. Pay includes annual retainer, meeting fees, stock-option value at the date of grant, and pensions for outside directors. Crystal looked at pay from 1993 to 1995 to smooth out the impact of a large option grant awarded in one year. The study didn't, however, tally the benefits of such perks as insurance, one-time grants of stock options for new board members, free cars, or travel. Crystal then compared the average pay of each director to the company's average performance, measured by stock appreciation and reinvested dividends over three years.

The average annual pay for an outside director was \$44,000, ranging from a high of \$368,000 at Minnesota-based HMO concern United Healthcare Corp. to a low of just \$550 a year for the outside directors of National Presto Industries Inc., an appliance maker in

Wisconsin. The overall averages lead some boardroom observers to argue that many directors are underpaid. "A good number of companies are underpaying for the time and effort directors now have to spend on the complex issues they deal with today," says John M. Nash, president of the National Association of Corporate Directors (NACD).

That's less true, however, when companies shift more pay to stock-option grants. And almost all of the largest pay packages include hefty grants urged on companies by corporate-governance activists who say options align the interests of directors and shareholders. Indeed, a 1995 NACD task force recommended that companies pay at least 50% of director fees in equity, with an eventual goal of paying 100% in stock. Crystal found that 39% of companies now grant stock options to outside directors, up from 29% a year ago.

STINGY? Today, most companies still provide rather small option packages to directors. Bell Atlantic Corp. and Federal Express Corp. award options for just 1,000 shares annually to their directors. But some companies—especially many of those that landed on Crystal's overpaid list—are giving out much larger options. Consider United Healthcare's outside directors. While board members there now receive an annual retainer of just \$20,000 and \$1,500 extra for every board meeting they attend, stock-option grants have made a huge difference. In 1993 and 1994, directors got option grants of as many as 64,000 shares, worth nearly \$750,000 in total. Last year the company became a bit stingy, handing out options on 16,000 shares worth \$274,900.

That's a bit of a cutback. But it's still better than a crisp C-note under a plate.

By John A. Byrne in New York



DALLAS SEMICONDUCTOR

OUTSIDE DIRECTORS'
AVERAGE ANNUAL PAY

\$195,200

OVERPAID BY

559%

Raking It In

COMPANY	OUTSIDE DIRECTORS' AVERAGE ANNUAL PAY 1993-1995	OVERPAID BY PERCENT*
DALLAS SEMICONDUCTOR	\$195,200	559
UNITED HEALTHCARE	368,000	549
CRACKER BARREL	202,900	440
WMS INDUSTRIES	163,800	422
CENTOCOR	97,300	256
NATURE'S SUNSHINE PRODUCTS	99,300	251
M. A. HANNA	141,800	247
SOUTHWESTERN ENERGY	88,900	241
ANADARKO PETROLEUM	118,000	233
LAWTER INTERNATIONAL	80,300	221

*Adjusting for company size and stock performance. Includes the value of stock options at the time they are granted.

DATA: GRAEF S. CRYSTAL

EDITED BY KELLEY HOLLAND

MCI DIALS M FOR MEXICO

TELÉFONOS DE MEXICO, THE telephone monopoly, long has been better known for surly operators and crackly lines than for customer service. But thanks to new competition, that may change. On Aug. 12, Avantel, a venture between MCI and Banamex, Mexico's biggest bank, started a service for big corporate clients with a 3,400-mile fiber-optic network linking 33 Mexican cities to the U.S. and Canada. Competition in residential long-distance begins in January, and seven other companies plan to invest nearly \$7 billion in the next five years to get into the market. So, even though Telmex recently offered 20%

discounts on long-distance calls, it may still be vulnerable. Mexico's long-distance market is expected to nearly triple, to \$11 billion, in the next five years.

BRAWLING OVER TRAWLING

GREENPEACE IS PLAYING chicken with fishing companies. The environmental group says trawling operations, which it dubs "strip-mining of ocean resources," indiscriminately capture millions of creatures and fish. The activists plan protests starting Aug. 15 in which they will use Zodiac boats to chase the giant trawlers and confront them at sea. A spokesman for American Seafoods, owner of a major trawler fleet, calls Greenpeace's criticism "ludicrous" and says the industry is thoroughly regulated.

CAN HE GET SNAPPLE CRACKING?

A NEW AGE DRINK IS GETTING a hard edge, as Michael Schott signs on as president of besieged Snapple Beverage. Schott, previously sales vice-president of Nantucket Nectars, "pushes himself, and expects everybody else to do the same," says a former colleague. Schott, who declined to comment, spent just four months at his last job, but Nantucket co-founder Thomas Scott says he worked constantly with distributors and retailers to boost sales. Snapple could use a boost: It has been losing money for parent Quaker Oats since it was acquired in 1994.

THE LATEST POWER COUPLE

IT'S THE NEW MERGER RAGE. Electric and gas utilities are pairing power and pipe, aim-

HEADLINER: RANDY LEVINE

THIS RELIEF PITCHER MAY GET THE SAVE

Major League Baseball negotiator Randy Levine has done what several predecessors could not. He's on the verge of a contract—at last—with the players' union that would include a salary cap but preserve players' arbitration rights. Now he has to get a few owner holdouts, including the Chicago White Sox's Jerry Reinsdorf, and players' union chief Donald Fehr to make the few concessions needed to close a deal. The old contract expired in 1993.

Two sticking points remain: whether to credit players for the time they

spent on strike in 1994 and 1995, and whether to drop unfair-labor complaints they filed then. A vote will be set if a compromise is reached.



Levine said in a statement that "a lot of work is necessary to reach closure," but closing this deal should be relatively easy for the labor veteran. Earlier, as New York City's labor commissioner, Levine hammered out contracts with bus drivers, sanitation workers, and school custodians. Baseball players may be no easier to deal with. But Levine is willing to play hardball.

By David Greising

ing to reduce costs and boost profits by offering customers a choice of fuels. The biggest matchup to date came on Aug. 12 when two Houston companies—Houston Industries and NorAm Energy, a gas utility with operations spreading across six states—agreed to connect. The \$3.8 billion deal comes just weeks after Enron announced it would buy Oregon's Portland General. Houston Industries CEO Don Jordan says he expects NorAm's gas knowhow to open new channels in power trading.

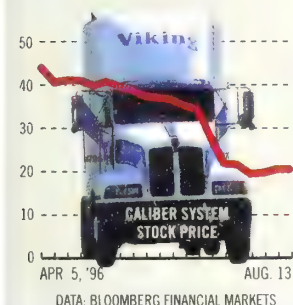
GUARDIAN'S ANGEL TAKES A FALL

IN JUST THREE MONTHS, Ollie North has gone from rags to riches to rags. After going public on May 14, share and warrant units in Guardian Technologies, priced at \$5.10 each, rose to close at \$12. North owns

nearly 15% of Guardian, a bullet-proof vest company of which he is also chairman and president. But Guardian's stock tanked in early August when its underwriter, Landmark International Equities, had to halt its market making because it failed to make a margin call. Landmark Vice-President Howard Berger says it expects to raise capital so it can soon resume trading. Meanwhile, Guardian shares and warrants are trading at a combined \$5.

ET CETERA...

- Munich Re is buying American Re for about \$3.3 billion to add to its U.S. presence.
- Ralcorp is selling Chex and other holdings to General Mills for \$570 million.
- Genzyme won FDA approval for a new membrane for use in surgery.
- American Express hired Richard Goeltz as CFO.



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EDITED BY OWEN ULLMANN

THE BIG BIZ-SMALL BIZ SPLIT OVER CAMPAIGN GIVING

NWith Republican control on Capitol Hill tenuous as the election approaches, you'd think the business community would be rallying behind its GOP soulmates in Congress. Think again. Small business is going all out to help finance vulnerable candidates, particularly House GOP freshmen. At Corporate America is another story. Sensing a shift in the political winds, big-company chiefs are shifting the allocation of their campaign donations between the two parties.

Indeed, Big Business could give Democrats a financial edge when November draws closer. And that's not sitting well with the Republican Congress, which sees treachery in boardroom pragmatism. "There's a lot of hedging going on, and Hill Republicans are really alarmed," concedes one corporate lobbyist. What's more, Corporate America's bipartisan largess could widen the divide between big and small business.

After the landslide of 1994, Big Business spent much of 1995 making amends for years of bankrolling ruling Democrats with an outpouring of support for the GOP. At the insistence of the new power brokers, Corporate America turned on the money faucets—especially for GOP House freshmen who came to Washington with heavy campaign debts.

Now, that flow is being diverted. In 1995, major corporate CEOs gave only 26% of their money to Democrats. By March 1996, that rose to 32%, according to the Federal Election Commission. A *BUSINESS WEEK* analysis of corporate giving through April, 1996, shows the trend continuing. Examples: AT&T has given 46% of its donations to Democrats in 1996, compared with 32% in 1995. Federal Express Corp. has given 50% of its money to Dems in 1996, up from 29% in 1995.

By contrast, small-business advocates, led by groups such as the National Federation of Independent Business (NFIB) and the National Association of Homebuilders (NAH), are funneling

even more money into GOP coffers. The homebuilders, for example, have given 86% of their money to Republicans this year, up from 83% in 1995. The Petroleum Marketers Association of America has followed suit, giving 92% of its contributions to the GOP this year, up from 86% in 1995. "They've been there on our issues," says John Kinan, the NAH's PAC manager. "We're going to be there for them."

DIFFERENT CONCERNS. For many small businesses, fearful of a return to a pro-regulatory Democratic Congress, it's not a matter of loyalty but one of survival. "It's a classic example of Big Business being able to survive in any climate," fumes

Jeffrey Butzke, PAC manager for the NFIB. "Small business suffers under all the regulations that are passed."

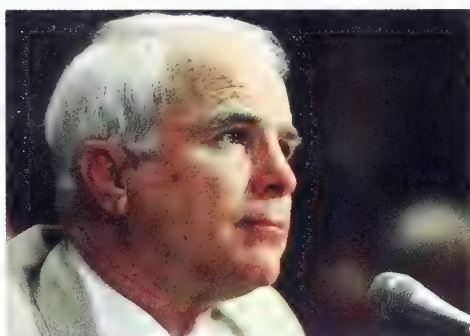
Corporate America has a different take on political matters. "Big Business isn't worried about ideological battles," says Marty Farmer, PAC manager for Barnett Banks Inc. Adds Robert G. Liberatore, Chrysler Corp.'s vice-president for Washington affairs: "A company with millions of shareholders can't afford to be partisan."

Still, Corporate America risks getting the cold shoulder for pet projects if an angered GOP holds control of Congress.

"They are notorious for leaning whatever way the wind is blowing," gripes Senator John McCain (R-Ariz.) But this time, warns Frederic V. Malek, an investment banker and top GOP fund-raiser, "Big Business is making a huge mistake."

Of course, now that polls suggest a resurgent GOP, Corporate America may shift its giving again. But it could be too late. A well-financed coalition of labor and trial lawyers is determined to return Democrats to power. And the Dems are certain to get a boost with voters from their confab in Chicago. A divided business community can only help that cause.

By Mary Beth Regan in Washington



McCAIN: Slamming fair-weather friends

CAPITAL WRAPUP

A NEW HEAD FOR THE NEC?

► North Carolina investment banker Erskine B. Bowles may return to the White House as a top economic adviser to President Clinton, Washington insiders say. Bowles, who had served as the President's deputy chief of staff and head of the Small Business Administration, returned to his Charlotte firm this year. Now, Clintonites report that he's a top choice to succeed National Economic Council Director Laura D'Andrea Tyson, who is expected to depart by yearend.

THE HILL'S PATENT OFFENSE

► Business is up in arms over Congress' attempt to grab money from the Patent & Trademark Office. The PTO's entire budget comes from fees levied on patent applicants and holders—some \$716 million for 1997. But Hill appropriations committees say that's too much. So they've skimmed off \$54 million for such programs as legal services and antiterrorism. Companies and inventors vow to fight the diversion when the spending bills come up for a final vote this fall.

NASA'S 800-POUND GORILLA

► For years, NASA has shrugged off scientists' predictions of big cost overruns on the \$17 billion space station, which would then eat into the budgets for other space projects. But now, the agency's claims that the station can be built within its original allocation are ringing hollow. Problems with the structural integrity of key station parts will be costly to fix. So NASA may have to tap into money that had been earmarked to build science facilities.

GERMANY

A MERCEDES FOR EVERY DRIVEWAY?

The builder of big-ticket luxury cars is trying to revamp itself into a full-range auto maker

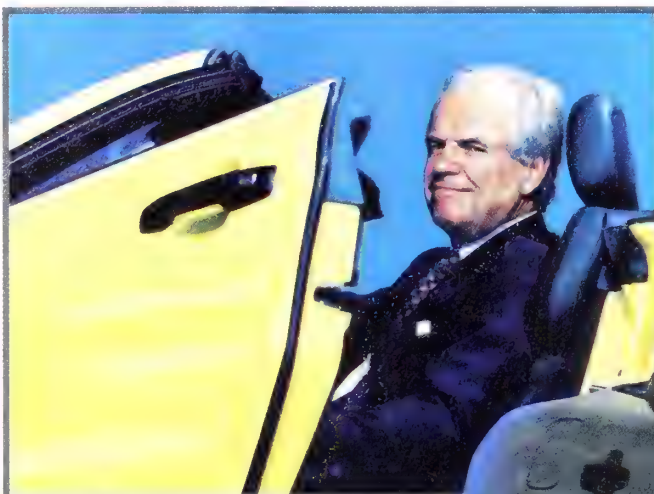
As he roars down twisting Italian country roads in a sleek new roadster, Helmut Werner is having the time of his life. "I have the best job in the world," grins the trim 59-year-old, speeding past Tuscan vineyards in an open-top Mercedes SLK.

As chief executive of Mercedes-Benz, Werner has a lot more fun than desk-bound CEOs. Test-driving, of course, is part of the job description. And he has a lot to be happy about. Three years into his tenure as Mercedes' chief, he has wiped away the huge losses of 1993, restored profit growth to this Daimler Benz unit, and boosted productivity dramatically.

More important for car buffs, he has brought excitement back to Mercedes, which had been sinking—slowly but perceptibly—under the weight of high production costs, out-of-control pricing, overengineering, and just plain stodginess. Consumers are begging for the right to buy the SLK, which sells for around \$40,000 fully loaded, a bargain by Mercedes standards. The convertible, with a retracting steel roof that folds into the trunk, debuts this fall. But you'll have to take a number. The production run of 35,000 is already sold out until 1998. "Cars are emotional things," says Werner, "and this is the most emotional product in our current lineup."

BOOMER BOUND. But even this natural optimist knows he has a tough road ahead. The former tire salesman is racing to transform this builder of big-ticket luxury cars into a full-range auto maker with a product in every segment. So his grand makeover has only just begun.

Werner does not want Mercedes to enter the next century relying too heavily on big, ultraluxury models such as its famous S-Class sedan. That's a very profitable business when done right, but it has its limits. Growth in the overall



HELMUT WERNER

The CEO had all his managers draft resignation letters. The message: Your jobs depend on how much you help transform the company

market for luxury cars is slow, even when you throw in rising sales in emerging markets. And in the developed world, buyers' ages fall too often in the 50-plus category. If it stays exclusively with luxury, Mercedes could risk becoming like General Motors Corp.'s Cadillac Div., stuck with the defeating image of "the car your parents drive." Although Mercedes has recovered from the initial attacks by Toyota's Lexus in the U.S., Werner knows the Japanese are relentlessly pursuing the goal of more luxury in a car at a lower cost. And many baby boomers are now comfortable with the idea of buying a Japanese luxury car.

The SLK, which is aimed at affluent fortysomethings, is one part of Werner's breakout plan to reach younger buyers who have made cars such as BMW's Z3 hot sellers. But he's envisioning far bolder changes—changes no one would have thought possible at Mercedes just 10 years ago. Werner wants new customers who covet Mercedes quality but need cars that can be versatile leisure vehicles as well as family runabouts, that tackle rough terrain or city streets, and

that offer the best in safety. So he's thinking small, as in small cars that will attract a whole new universe of buyers to the Mercedes brand and double car sales, to 1.2 million, within five years. Archrival BMW shot past Mercedes, to 1 million cars a year, by taking over Britain's ailing Rover Group Ltd. in 1994. Werner is doing it the hard way—by internal growth.

At the fall, 1997, Frankfurt Motor Show, Mercedes will unveil its new A-Class, the smallest car it has ever made, 11 feet long and priced at about



Critics fear the avalanche of models could just end up doubling unit sales and cutting profits in half

0,000 in Germany. In 1998, in a joint venture with Switzerland's SMH Swatch watchmaker, Mercedes will launch the 0,000 Smart microcar—just 7.5 feet long—for city travel, aiming to capture affluent Europeans who want an environmentally correct second car. Swatch CEO Nicholas G. Hayek brags that the Swatchmobile "is designed for 'two people and a crate of beer.'"

AND DRIVE. Mercedes plans to make 0,000 units of each a year in Europe. Together with the M-Class four-wheel-drive being made in Alabama that will

will make many more product lines."

Werner loves playing the game. A sports enthusiast who swims, skis, cycles, and plays tennis, he nearly ended up as a bean counter. The eldest of five sons of a successful bank director, he embarked on the arduous seven-year training of a German auditor. After the first stage, he recalls: "My professor told me to go get some real-life experience first." The resulting trainee job with tiremaker Uniroyal was a turning point. As soon as he hit the road as a salesman, he was in clover. Even now, he's never happier than when peddling the product.

Critics fear that the supercompetitive Werner could just end up doubling unit sales and cutting profits in half. They are quick to

Werner's ambitions don't surprise his friend and business associate Roger S. Penske, chairman of Detroit Diesel Corp., in which Daimler owns a 20% stake. "He is a risk-taker," says Penske. Yet some analysts think Werner may have overreached himself in projecting demand for his small cars. DRI/McGraw-Hill consultants in London forecast that sales of A-Class sales could peak at 125,000 units in 1999, far short of the 200,000 European production capacity, because of competition in the segment. And BMW rejected the idea of building a small two-seater sedan because "the possible uses of such a car are very limited," says a BMW source. "Instead of sticking to what they know in luxury markets," complains Thomas R. Holmes, a partner in Frankfurt private bank Schröder Münchmeyer Hengst (SMH), "[Mercedes] will be making something that everyone else makes."

Not so, retorts Werner. Still the dedicated salesman, he'll tell anyone willing to listen that the A-Class constitutes an entirely new market segment of premium or luxury small cars. It certainly looks different. The body is short but high, making it as roomy inside as an E-Class. The engine is placed so that it will dive below the car's floor toward the road in the event of a head-on collision, rather than being projected toward passengers as in conventional designs. Some outsiders agree with Werner. "It's not just a new small-car-market entry—it has a distinct character," says former Ford Motor Co. executive Karl E. Ludvigsen, now chairman of London consultancy Ludvigsen Associates.

The key question is whether Mercedes has the cost discipline to profit on small cars. Five or 10 years ago, they would probably have failed. But now, says Ludvigsen, "they have the tools to bring the program home on budget. That would not have been possible in the pre-Werner era."

In 1993, when Werner took over, Mercedes had slumped into an \$800 million loss, the big-selling E-Class and C-Class models were eight and 10 years old, and production barely topped 500,000 cars. The company was bloated

MERCEDES SLK

Priced at \$40,000 fully loaded, the convertible is already sold out until 1998



but in 1997, the new models will turn Mercedes into a full-range carmaker of 2 million passenger vehicles a year. Says Werner: "We have to learn to make money from small runs of exclusive cars."

Over the next three years, Mercedes will splash out \$16 billion in capital spending and research and development, a third for new car models alone. Even then, the model avalanche won't stop. According to local reports, Mercedes will churn out nearly 30 new models by 2008. Werner refuses to comment on the reports, but says: "We

point out that it wasn't long ago that Mercedes could barely eke out profits on its core luxury franchise. How can it earn a decent margin on small cars when mass producers such as Fiat and Volkswagen often struggle? Internal documents suggest that Werner's brand extensions, such as the A-Class, will lower overall return on investment. All the same, they lay out daunting goals: By the end of the century, Mercedes' sales could soar 40%, to \$67 billion, and net profits nearly triple, to \$3.6 billion, with an unchanged workforce.

with six layers of managers between the board and the shop floor. Werner slimmed that to four, because hundreds of managers, according to studies by consultant McKinsey & Co., cost more than they contributed in revenues.

Plant managers were made responsible for containing their own expanding budgets. And once they had to answer for spending, they dropped their bad old macho habits of amassing the biggest budget possible. In one exercise, Werner had all his managers draft letters of resignation. The message: Your jobs depend on how much you help Mercedes' transformation.

The biggest challenge was to reinvent the corporate culture. Long dominated by engineers, the old Mercedes approach was to build the best possible car regardless of expense and then set the price by adding a profit margin to ballooning costs. Werner flipped that strategy, fixing a target sticker price and then building to that. Explains passenger-car division head Jürgen Hubbert: "We had to break the assumption that each new car had to be heavier, have even more technology—and be more expensive."

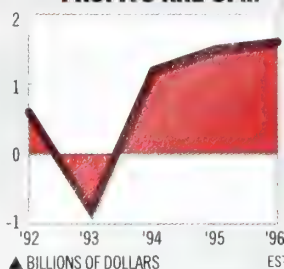
It had to come. By 1990, Mercedes confronted shocking evidence from Massachusetts Institute of Technology's International Motor Vehicle Program (IMVP) and studies by McKinsey that since 1985, a huge 35% productivity gap had opened up between it and Japanese producers such as Toyota.

BIG GAINS. Werner told his engineers to simplify manufacturing fast. As a result, productivity has risen 30% over the past two years, and \$2.3 billion has been saved. The big gains come from major model changes that allow extensive redesign and cost purging.

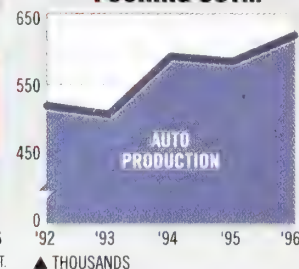
As a result, Mercedes was able to price the C-Class in the U.S. at \$29,900, or \$700 less than the competing Lexus ES300. Five years earlier, the comparable Baby Benz 190 cost \$9,800 more than the entry-level Lexus ES250.

Solving the problems in the U.S. was a critical test of the new Mercedes' skills. By 1993, Mercedes-Benz North America marketing chief Michael Jackson was urgently pressing his German bosses to revamp the Mercedes image in the U.S. "We needed to connect to the baby-boom generation," says Jackson, a

MERCEDES-BENZ PROFITS ARE UP...



...THE CARS ARE POURING OUT...



...AND NEW MODELS ARE COMING

Scheduled introduction of all-new or redesigned models

INTRO YEAR	CLASS	CAR TYPE	BASE PRICES
1996	SLK	roadster	\$35,300
	V-Class	van	35,400
	C-Class	station wagon	33,100
1997	E-Class	station wagon	43,100
	A-Class	small, van-like car	20,000 *
	CLK	coupe	40,000 *
1998	M-Class	off-the-road vehicle	35,000 *
	Smart	"Swatch" micro car	10,000 *
	S-Class	large luxury sedan	63,000 **

* Target price
** BW estimate

German sticker prices including tax

former dealer himself. "We needed to get people to say Mercedes-Benz is the best car for me." That meant lowering the price to attract the 40-plus buyers. But it also meant catering to the quirks of the American market. In one episode, U.S. dealers pressed the puzzled Germans for cup holders. Now the E-Class sedan sports a nifty retractable one.

Mercedes also made a radical change in advertising, from the formal, reverential ads that stressed engineering to ones that used humor to reach out to boomers. Ad agency Lowe SMS now has spots featuring a Mercedes navigating through a herd of rhinos and another using Janis Joplin's '60s refrain, "Lord won't you buy me a Mercedes-Benz." Mercedes car sales in the U.S. are up 17% for the year.

Werner will have to keep on running hard. Japanese competitors are keeping the pres-

sure on. Nissan Motor Co. and Toyota, makers of the Infiniti and Lexus, aim to make 30% to 50% savings on each model. Toyota, for instance, cut costs \$1.2 billion last year, boosting profit nearly 14% despite a decline in sales. Says UBS Securities Tokyo-based auto analyst Peter Boardman: "The Germans are going after a moving target."

SOFTER DEMAND? Still, Werner's mix of new models and pricing is resulting in record first-half sales of 315,000 cars, up 7.2% from the same period of 1995, and booking \$15 billion in revenues, a 12% rise. The second half will be tough, as demand in Western Europe softens. But Werner is promising profits up to 1995 levels.

Like other auto makers, Mercedes is rushing to spread manufacturing around the world. It urgently needs to tap into new markets for trucks and cars. And it must find both new and cheaper sources of supplies and new manufacturing sites, such as in China and India. Werner's ambitious goal is to raise the proportion of cars Mercedes makes outside Germany to 25% over the next 10 years, from just 5% now.

Small cars. Swatch cars. New sales techniques. Plants in China. The list of new ventures and efforts Mercedes must quickly master is long, especially for a company where redesigning a simple headlight once took months. Says Susan G. Jacobs, president of consultant Jacobs & Associates in Rutherford, N.J.: "It is a bigger mistake for Mercedes to make one change too little than one change too many." Changing too little is one thing Helmut Werner will never be guilty of.

By John Templeman in Stuttgart, with Bill Vlasic in Detroit and Christopher Power in New York

M-CLASS

The four-wheel-drive model will be built in Alabama



BIG BUCKS FROM BIGGER BOATS

So far, Fincantieri's survival-of-the-glitziest strategy pays off

The bigger and glitzier cruise ships get, the better Corrado Antonini likes them. As chief executive of Italian state-owned shipbuilder Fincantieri, Antonini has turned the company from a subsidy-swilling white elephant into the world's No. 1 builder of cruise liners. Its latest creation, the *Carnival Destiny*, commissioned by the Miami-based cruise king Carnival Corp., loaded with 280 tons of Italian marble and a two-ton Venetian chandelier in its three-level indoor theater. Carrying 400 people, it will be the largest cruise ship ever built when it is completed this fall.

The 62-year-old Antonini took a gamble when he pinned Fincantieri's fortunes to the cruise craze that began 10 years ago. So far, the bet has paid off. But to remain successful, Fincantieri must keep a step ahead in an industry that some observers think is already facing oversupply. Antonini's answer: Build ever-bigger, ever-louder ships.

MIKEY'S STATUE. That's what Fincantieri's customers seem to want—even more than a low bill. Says Carnival Chairman Micky Arison, who ordered Fincantieri a contract for two more vessels last month: "Because they understand what we need, they don't have to be the lowest bid." Pleasing its clients helped Fincantieri turn a profit of \$6.8 million in 1995, compared with a loss of \$79 million in 1992. Antonini's test coup: a reported \$1 billion contract signed last year with Walt Disney Co. to build the first two vessels for

its new cruise unit. The *Disney Magic* and *Disney Wonder*, two mock-1940s steamliners, will be adorned with images of Mickey Mouse and other Disney characters, and a bronze statue of Mickey will stand in the ships' main atrium. The ships will take passengers on week-long cruises to the Bahamas, with stops at Disney's private desert island, Castaway Cay, and Disney World in Orlando.

This is heady work for a company that used to build mostly warships and tankers. Shipbuilders throughout Europe are closing shop, victims of re-

BOUND FOR DISNEY WORLD: DISNEY IS BETTING A BILLION ON THE CRUISE BUSINESS



duced government subsidies, hefty cuts in defense spending, and pressure from East Asian competitors. Meanwhile, Fincantieri boasts an order book worth \$6.2 billion that is so dense it can't accept any new cruise shipbuilding contracts until 1999. Such ships take around two years to build.

CEO and President Antonini was largely responsible for steering Fincantieri into profitability. In the mid-1980s he initiated a huge turnaround effort, dropping duplicate or unproduc-

tive shipyards, streamlining production, and slashing the workforce from 30,000 to 11,600. His biggest gamble, entering the cruise boat business, fortunately coincided with the start of America's *Love Boat* fever and the scramble among cruise companies for huge, snazzy ships. Throw in the 1992 lira devaluation, and Fincantieri was able to roar ahead.

Part of its success is that Fincantieri can offer high-quality design and high-tech features at competitive prices. By linking up with the network of small businesses in Italy's booming northeast, Fincantieri can keep down the costs of outfitting a ship with the glass, marble, leather, and electronics that together account for the bulk of total construction costs. This network of small, flexible subcontractors also provides cutting-edge technology. So Fincantieri can offer its clients attractive features such as a funnel that blows smoke away from passengers and a noise-reduction system that diverts the engine's vibrations away from the ship.

The honeymoon may not last much longer. Analysts believe the cruise ship industry may be heading for a slowdown as passenger volumes level off and ship capacity keeps skyrocketing. "The ships currently on order may be far in excess of what the industry can digest," warns James R. McCaul, a shipbuilding analyst with IMA Associates in

Washington.

For now, Fincantieri is following the cruise industry's strategy of making each ship more gigantic than the last. Its latest undertaking, the *Grand Princess*, commissioned by London-based P&O Group, will be even bigger than the *Destiny* when it hits the seas in the spring of 1998. But for Fincantieri to keep steaming ahead, Antonini will need to spot the next hot shipbuilding niche before competitors get there first.

By Monica Larner in Trieste

Fincantieri's Super Cruisers

NAME OF SHIP	PURCHASER	PRICE	DELIVERY DATES	DESCRIPTION
DISNEY MAGIC AND DISNEY WONDER	Disney Cruise Line	\$506 million each	Jan. 1998 and Nov. 1998	Modeled after 1940s classic transatlantic liners. Crew will be dressed as Disney characters in the children's area. Will carry 2,400 people.
CARNIVAL DESTINY	Carnival Corp.	\$553 million	Fall 1996	World's largest cruise ship. Will carry 4,400 people and have 1,320 cabins with ocean balconies.

DATA: FINCANTIERI, WALT DISNEY CO., BUSINESS WEEK



Tom LaFleur
Vice President, QUALCOMM Incorporated
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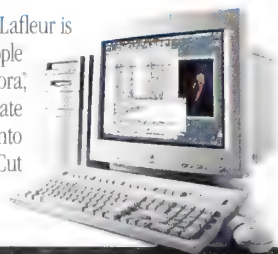
Where questions never go unanswered.
Where the people you need to find can always be found.

Where information forever eludes the bottleneck.
And misunderstanding has taken a leave of absence.

IT'S A PLACE CALLED THE INTRANET.

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As V.P. and resident visionary for QUALCOMM—one of the brightest stars in digital wireless communications—Tom Lafleur is finding innovative ways to stay ahead of his company's phenomenal growth with the help of the WorldWideWeb and Apple Macintosh® computers. In fact, Tom started QUALCOMM's Intranet by running one of their own products on a Mac®—Eudora®, which has since become the most popular e-mail software for the Net. Today, people are using Macintosh to easily create web pages and share details of their projects with the rest of the organization. So engineers have instant insight into manufacturing problems, can pull up drawings and quickly resolve issues. Which has slashed the need for paper. Cut support costs. And sparked unprecedented collaboration. Not to mention knocking a few walls down along the way.



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By Peter Engardio

IS THE EAST ASIAN JUGGERNAUT SPUTTERING?

From Seoul to Singapore, Asians accustomed to thinking of themselves as immune to economic downturns are starting to wonder. After years of torrid growth, Tigers are suddenly reporting sharply slower exports, deteriorating current accounts, and lower gross domestic product forecasts. In South Korea, the finance minister has been forced to resign over a record first-half current account deficit of \$9.3 billion. In Thailand, export growth in the first half plunged from 23.4% in 1995 to 4.4%, and the current account gap is

port-led model needs an overhaul. One problem is the overcapacity in next-generation industries. Much of the region is counting on petrochemicals, autos, consumer electronics, and semiconductors to move up the value-added ladder as they lose their cheap-labor advantage in garments, shoes, and toys. South Korea and Taiwan are scrambling to catch up with Japan. And China, Indonesia, Malaysia, and Thailand are vying to be the next South Korea and Taiwan.

But East Asia's technocrats may have miscalculated. Clearly they have

ty than their markets can absorb. It's a similar story in telecom equipment and computer peripherals. Says Standard Chartered Bank's economist Kwok Kwok-chuen: "Overcapacity is becoming conspicuous. Ultimately, there will be a shakeout."

YEN AGAIN. Misjudgment of the yen is one reason why East Asia's Tigers overexpanded. When the yen hit 80 to the dollar last year, even many companies in Japan moved production elsewhere in the region. But since then, the dollar-pegged currencies of South Korea, Taiwan, Thailand, and China

have gained more than 20% against the yen.

Most economists believe that as Japan gets rolling again, the yen will rebound and East Asia's export woes will vanish. What's more, most Tigers are likely to cushion themselves by broadening their currency baskets to include more yen. But such fluctuations are only part of the story, contends Kenneth S. Courtis, Tokyo-based chief economist for Deutsche Bank Capital Markets Asia. Thanks to corporate restructuring, Japan may not cede

While some economists point to cyclical factors, others believe the region's problems are structural

A MITSUBISHI FACTORY
IN KUALA LUMPUR,
MALAYSIA



expected to hit \$15 billion by yearend. In China, exports actually dropped 8% after gains of 32% and 23% in 1994 and 1995.

The downturn has sharpened a debate among economists. A few Westerners, such as Paul Krugman, argue that the region is having a hard time finding growth through greater productivity and technological innovation. The big gains from capital investments and mass mobilizations of workers are over, they maintain. But many more economists argue that the downturn can be explained by cyclical factors such as currency fluctuations, a plunge in semiconductor prices, and policy changes in China. Asian economies should be humming nicely by next year, they predict.

Certainly it is far too early to say that the East Asian dynamo is finished. Still, as Asians gaze into the future, they should see that their ex-

overshot global demand. Perhaps more important, they may have been too hasty in assuming that Japan and the West would walk away from these industries. The troubles facing South Korea can't be encouraging. Some of the hardest-hit sectors were semiconductors, petrochemicals, and steel, which accounted for 28% of 1995 exports. In each, says Lee Kyoung-Sook, a researcher at the Korea Institute for Industrial Economics & Trade, "oversupply pulled prices down."

True, few anticipated the falloff in demand that led to this year's 60% crash in memory-chip prices. But even if demand picks up, prices will be depressed by the dozens of wafer fabs going up in Singapore and Taiwan. In autos, Hyundai, Daewoo, Samsung, and Kia are boosting output. But China, Thailand, and Indonesia, all vying to be Asia's new export base, are adding more capaci-

as much industrial base as expected. "The Japanese haven't been navel-gazing for the past four years," says Courtis. "They've cut costs."

If South Korea is having a hard time competing as a cheaper Japan despite its highly skilled work force, giant industrial groups, and a decade of experience in high-end exports, what does this say for the likes of Thailand, Malaysia, and Indonesia? They had better focus more of their industrial policies on their consumers, rather than counting on foreign markets to soak up their excess output. This summer's export slowdown could well turn out to be a blip. But if megafactories keep going up at the same pace, it could look mild compared to a more wrenching shakeout that looms in the future.

Asia Correspondent Engardio covers the region from Hong Kong.

DITED BY PAULA DWYER

INDONESIA: SUHARTO MAY WIN THIS BATTLE, BUT NOT THE WAR

After 31 years of authoritarian rule, ailing Indonesian President Suharto is looking more desperate with each passing day. In mid-August, the 75-year-old military ruler launched a sweeping crackdown on pro-democracy and labor leaders. He reshuffled the military top brass, kicking a general who failed to anticipate riots in which thousands of middle-class Indonesians took to the streets of Jakarta in late July. Suharto also installed his son-in-law as commander of an army unit expected to restore order and protect the family fortune.

The President's next move, say diplomats in Jakarta, will be against prominent opposition leader Megawati Sukarnoputri, a former housewife turned firebrand of an embryonic democracy movement. Megawati already has been removed from the chairmanship of her Indonesian Democratic Party (PDI) and summoned twice for "questioning" by police. Sources expect the police will find some way of restraining her, whether it's by placing her under house arrest or taking away her legal rights.

Megawati can expect to be accused of inciting riots in an alleged conspiracy with the outlawed Indonesian Communist Party. Those are the charges against 10 pro-democracy activists and a labor leader who have been arrested. Giving Megawati the same treatment could provoke more riots and lead to bloodshed. Some troops are still patrolling the capital with submachine guns.

Suharto's handling of Megawati thus far shows that he is ill-equipped to face legitimate opposition from a politician with popular support. She was once perceived as merely boasting a powerful family name, as daughter of former President Sukarno, who was ousted by Suharto in 1965. But Megawati is building up a grassroots base for the PDI. "She sees a need to connect with the masses. That's what's going to power her party

and bring in votes," says a diplomat in Jakarta. Suharto's ruling party, Golkar, which wins a majority every five years by preventing opposition parties from getting equal campaign time, looks like an obvious fraud in comparison.

Bereft of popular support, Suharto is closing ranks with his military allies and weeding out possible opponents before the 1998 presidential election. He is expected to move faster than usual to nominate a vice-president, a post traditionally filled by a Javanese army general.



MEGAWATI: Pro-democracy leader

Megawati, 49, isn't the only pro-democracy leader who has been targeted. Muchtar Pakpahan, jailed in 1994 for allegedly inciting factory workers' riots in North Sumatra, was arrested again in late July. Budiman Sudjatmiko, and nine other leaders of the People's Democratic Party, were also arrested Aug. 11 and 12. Muchtar and Budiman are charged with the capital crime of sedition and inciting riots. They have denied they are communists.

Jakarta is braced for repeats of the July riots that rocked the city. Juwono Sudarsono, professor of political science

at the University of Indonesia, says the July rampage resulted from "cynicism and outright rejection" of Suharto's regime, "especially among the young and unemployed."

The only comfort for Suharto may be knowing that his six grown children and their extensive business interests could be protected. His newly elevated son-in-law, Prabowo Subianto Soemitro, can be expected to stand guard over the family fortune. Prabowo's rise to major general, at the young age of 44, is his second such promotion in a year. The U.S.-trained commander could prove to be a valuable asset if Suharto's health worsens, and could even emerge as his successor—but that promises to be a rocky transition.

By Michael Shari in Jakarta

GLOBAL WRAPUP

TURKEY LOOKS EAST

► Turkey's new Islamist Prime Minister, Necmettin Erbakan, seems intent on steering his country toward closer relations with Muslim nations. That could test his country's long-standing ties to the West.

Erbakan went to Tehran Aug. 11-12 to sign an agreement to import \$20 billion worth of natural gas from Iran, just days after President Clinton signed the Iran-Libya Sanctions Act, designed to discourage foreign companies from investing in those countries'

oil and gas industries. Erbakan also irked the U.S. by announcing his plans to strengthen Turkey's ties to Iraq and Syria.

Turkish officials say the gas deal does not violate America's new sanctions law, since it doesn't call for direct investment in Iran. American officials may accept this as an excuse not to impose sanctions on a vital NATO ally. But Turkey's increasing closeness with states that the U.S. sees as sponsors of international terrorism seems certain to strain future Turkish-American relations.

LABOR SEES RED IN TORY ADS

► Advertising guru Maurice Saatchi's latest Conservative Party ad campaign has London buzzing. One ad superimposes a pair of slanted red eyes on Labor Leader Tony Blair's smiling face. Another shows a sinister, red-eyed figure. Both are captioned: "New Labor, New Danger." The message: Blair is a socialist devil. The media panned the ads, but Tories like the attention. A recent poll put Labor just 12 points ahead, compared with 21% in April.

STRATEGIC

After a decade of gritty downsizing, Big Thinkers are back in corporate vogue

He was in his mid-20s and had never made a product, run a business, or managed an employee. But he was armed with a Harvard University MBA and a power suit, and he had a magic talisman: He was a consultant at one of the hottest strategy boutiques of the 1970s. And after he completed a presentation on Boston Consulting Group Inc.'s strategic ideas at a major U.S. company, the young consultant got his due when the board of directors erupted into enthusiastic applause.

Those were heady times, recalls John Clarkeson, the young MBA who joined BCG from Harvard in 1966 and is now its chief executive. In its heyday, strategy-spinning was the ultimate left-brain exercise for the corporate elite. Thousands of B-

school-trained thinkers sat high in the climate-controlled aeries

Cover Story

of bloated business empires, crunching numbers and spinning scenarios to conquer adversaries. The popularity of corporate strategy spawned a mini-industry of brainy consulting boutiques, and nearly every CEO worth his perks learned how to sort out his business by cows, dogs, stars, and question marks. Everything could be categorized, analyzed, quantified, and predicted. You could plot a strategy that would safely steer your company to uninterrupted triumph if only you *thought* hard enough.

Or maybe not. By the early 1980s, as U.S. companies found themselves battered by global competitors and more nimble entrepreneurs, the cerebral strategizing of the past looked like a luxury of a more leisurely era. Suddenly, Corporate America was frantically struggling to catch up. Instead of weaving elegant stratagems, companies were scrambling to improve quality, restructure, downsize, and reengineer.

But here's a funny thing. After more than a decade of shrinking to hike productivity and efficiency, companies are now eager to wring more profits out of those streamlined operations. So what's making a comeback? You guessed it: strategic planning. Suddenly, the idea of rising above the tumult of day-to-day business to ponder the future of markets and competitors is looking attractive again. Reengineering consultants with stopwatches are out. Strategy gurus with visions of new prospects are in. "The pure efficiency approach did very little to generate distinctive competitive advantages,"

says Dwight Gertz, a consultant at Mercer Management Consulting Inc., which says its growth-strategy business has nearly doubled in the first half of the year.

At one company after another—from Sears to IBM to Hewlett-Packard to Searle, strategy is again a major focus in the quest for higher revenues and profits. With help from a new generation of business strategists, companies are pursuing novel ways to hatch new products, expand existing businesses, and create the markets of tomorrow. Some companies are even recreating full-fledged strategic-planning groups. United Parcel Service expects to spin out a new strategy group from its marketing department, where strategic plans are now hatched. Explains Chairman Kent C. Nelson: "Because we're making bigger bets on investments in technology we can't afford to spend a whole lot of money in one direction and then find out five years later it was the wrong direction."

"REBOUND." Many mainstream consulting firms, including one-time strategy leader BCG, say their strategy business is booming. Meanwhile, a new wave of gurus and consulting firms has emerged with a wide assortment of perspectives and tools for companies to create strategy. A recent study by the Association of Management Consulting Firms found that executives, consultants, and B-school professors all agree that business strategy is now the single most important management issue and will remain so for the next five years. "We are seeing strategy make a rebound," says Vijay Govindarajan, a well-known strategy professor at Dartmouth College's Amos Tuck School of Business Administration. "Strategy has become a part of the main agenda at lots of organizations today."

But if strategic planning is back with a vengeance, it's also back with a difference. Gone are the abstraction, sterility, and top-down arrogance of the old model. The death knell for that approach was sounded in 1983 when General Electric Chairman John F. Welch dismantled the company's once heralded planning department, where as many as 200 senior-level staffers used to crank out vinyl-bound reports. Welch found GE planners too consumed with operating and financial details instead of competitive positioning and the creation of

val·ue mi·gra·tion n: The movement of growth and profit opportunities from one industry player to another

future markets and too divorced from the day-to-day reality of line managers.

Today's gurus of strategy urge companies to democratize the process—once the sole province of a company's most senior officers—by handing strategic planning over to teams of line and staff managers from different disciplines. Frequently, these teams include junior staffers, handpicked for their ability to think creatively, and near-retirement old-timers willing to tell it like it is. And to keep the planning process close to the realities of markets, today's strategists say it

PLANNING



Cover Story



“My role is to encourage discussion of the white spaces the overlap and gaps between business strategies”

LEWIS E. PLATT

Chairman, Hewlett-Packard

banking, satellite telephony, or genetic engineering,” says Gary Hamel, who, with colleague C. K. Prahalad, is among the most influential of the new breed of strategy gurus (page 50).

A good example of such a transformational shift is Procter & Gamble Co.’s decision four years ago to compete on the basis of low prices. That flew in the face of conventional strategic thinking, which argued that companies with premium brands never have to worry about being the low-cost producer in an industry. By challenging that widely held belief, P&G reinvented itself and its in-

dustry. Result: Profit margins are at a record 11.6%, up from 6.4% when the about-face in strategy occurred.

This wouldn’t be management if the new thinking about strategy didn’t come with a whole lexicon of new buzzwords. Forget about the value chain, experience curves, stars, and dogs. Now, any enlightened discussion of strategy is likely to include talk of “co-evolution” and the “business ecosystem”—creating networks of relationships with customers, suppliers and rivals to gain greater competitive advantage. Here’s how it sounds in practice: “In a global market, companies should learn how to work in a world of business ecosystems where they can get other players to co-evolve with their visions of

should also include interaction with key customers and suppliers. That openness alone marks a revolution in strategic planning, which was always among the most sacrosanct and clandestine of corporate activities. But it’s necessary if the process is to help produce what customers want.

It’s worth taking some risks to get the process right. When companies get their strategies wrong, the results can be disastrous. IBM’s failure to maintain its leadership in the personal-computer market, arguably one of the past decade’s biggest strategic blunders, cost Big Blue as much as \$90 billion in lost market capitalization, according to Adrian J. Slywotsky, a founder of Boston-based Corporate Decisions Inc. Slywotsky, one of several new thinkers in the field, estimates that the decision by former Apple Chairman John Sculley not to license the Macintosh operating system in the mid-1980s cost Apple Computer Corp. \$20 billion to \$40 billion in value.

Hoping to avoid a similar fate, Microsoft Chairman William H. Gates III is redirecting his strategy toward the Internet. “Every new change forces all the companies in an industry to adapt their strategies to that change,” says Gates. “But here

co-evo-lu-tion n: The notion that by working with direct competitors, customers, and suppliers, a company can create new businesses, markets, and industries

was clearly the case where if we sat around and didn’t recognize the thing and didn’t understand it, someone else would take leadership.”

If even Microsoft Corp.—an upstart just a moment ago—risks being whipsawed by ever faster change, it’s no wonder nearly all these new thinkers argue for bold strategic approaches to stay ahead of that change. Instead of being called upon to eke out fractions of market share or revenue growth, today’s gurus say, strategic thinking should be seen as an opportunity to transform a corporation and change the rules of an industry to its advantage. They decry incremental change. “Our view of strategy has shifted from the classic Coca-Cola vs. Pepsi market-share fight to how do you shape the emergence of the new opportunity arenas, whether it’s branchless

The Rise and Fall and Rise of Strateg

EARLY 1960s Harvard professors Ken Andrews and C. Roland Christensen articulate the concept of strategy tool to link together the functions of a business and assess company’s strengths and weaknesses against competitors.

EARLY 1960s General Electric emerges as the pioneer in strategic planning, creating a large, centralized staff of planners to ponder the future. Consultant McKinsey & Co. helps GE view its products in terms of strategic business units, identify competitors for each, and evaluate its position against them.



1963 Under founder B. D. Henderson, Boston Consulting Group becomes the first of many strategy boutiques. BCG pioneers a series of concepts that Corporate America by now includes the “experience curve” and the “growth market-share matrix.”



e future," says James F. Moore, founder and chairman of Partners Research Inc. in Cambridge, Mass.

You'll hear talk of "value migration," "strategic intent," "game theory," and "core competencies," too. "White-space opportunities" are also big. These are potential areas of growth that often fall between the cracks because they don't naturally match the skills of existing business units. The new strategists believe it's necessary to pay keen attention to these in order to focus on what can be rather than what is.

Tortured as the lingo is, these approaches are getting a welcome reception in Corporate America. Sears Roebuck & Co. found the idea of value migration to be a useful model for understanding its excruciatingly long decline. To strategy guru Slywotsky, value migrated throughout the 1980s from outmoded business designs of such retail incumbents as Sears and Montgomery Ward to new, more competitive ones such as specialty stores, superstores, and discounter stores that were better able to satisfy customers.

From 1985 to 1994, about \$163 billion of stock market value was added in the retail industry. Some 25 companies were responsible for creating 85% of that wealth, and many of them did it with "business designs" that featured stores outside shopping malls, with low prices, quality merchandise, and good selection. While Wal-Mart Stores Inc. generated \$42 billion and Home Depot Inc. added \$20 billion in value, Sears' retail operations captured less than \$1 billion in that year period.

HUGE HOLE. How did it happen? Like so many American business icons, Sears lost sight of its customers. "We didn't know who we wanted to serve," concedes CEO Arthur C. Martinez. "That was a huge hole in our strategy. It was also unclear on what basis we thought we could win against the competition."

A major strategy overhaul led to the disposal of nonretail

assets and a renewed focus on Sears' core business. Martinez renovated dowdy stores, upgraded women's apparel, and launched a new ad campaign to engineer a major turnaround at the department-store giant. But now, he has to prove he can make the business grow, a tough assignment since Sears is still essentially locked into relatively cramped mall-based stores. So a year ago, Martinez enlisted Slywotsky's Corporate Decisions to help Sears create a new future. "What I liked most about them is that they came at it from a customer perspective," says Martinez. "Strategy can sometimes be this inside-out, self-absorbed self-examination process. But they have an outside-in view of strategy. I was mightily taken with that, because one of the things that got the company in trouble was its lack of focus on the customer."

Extensive customer research discovered high levels of

white-space opportunity n: New areas of growth possibilities that fall between the cracks because they don't naturally match the skills of existing business units

brand loyalty to Sears' hardware lines. The research also suggested that by segmenting the do-it-yourself market and focusing on home projects with a low degree of complexity, say, papering a bathroom or installing a dimmer switch, Sears could avoid a major competitive collision with Home Depot and other home-improvement giants. Customers, the Sears research showed, desired convenience more than breadth of category in such hardware stores.

After successfully testing the concept of hardware outlets, Martinez is now making a billion-dollar capital bet that Sears can gain growth in this new market. He hopes to have 1,000 freestanding, 20,000-square-foot hardware stores built in five years, with 200 of them up and running by yearend, at a cost of \$1.25 million per outlet.

Other devotees of Slywotsky's precepts include Searle

Harvard professor Michael E. Porter's book *Competitive Strategy* is a genera-

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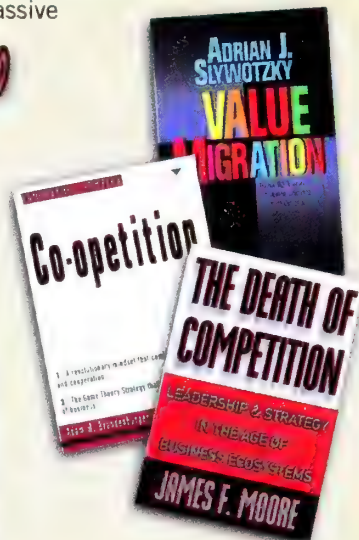
New GE Chairman Jack Welch slashes the corporate plan-group and purges scores of managers from GE's operating units. Numerous companies follow his

LATE 1980s Battered by global competition, companies turn away from strategic planning and begin to focus on operational improvement. Executives embrace the Total Quality Management and the teachings of W. Edwards Deming.

LATE 1980s Corporate America begins massive downsizing and reengineering of operations to increase efficiency and productivity. Guru Michael Hammer leads the reengineering revolution.



1994 After 10 years of downsizing, companies begin to focus on how to grow. Academics C.K. Prahalad and Gary Hamel become the most influential of a new group of strategists with the publication of *Competing for the Future*.



NOW A bevy of new books are out from a new group of strategy gurus who are capturing the attention of corporate executives and redefining the process of strategy creation.

DATA: BUSINESS WEEK

Pharmaceuticals, which is customizing strategies to deal more effectively with managed-care organizations in certain markets, and Philips Electronics, which is using his methodologies to help it make research-and-development investments for new technology-based products.

Cover Story

In turn, the notion of white-space opportunities is proving especially compelling for highly decentralized companies such as Hewlett-Packard Co. HP Chairman Lewis E. Platt now believes his most important role in strategy formulation is to build bridges among the company's various operations. "I don't create business strategies," argues Platt. "My role is to encourage discussion of the white spaces, the overlap and gaps among business strategies, the important areas that are not addressed by the strategies of individual HP businesses."

To bridge those gaps, HP now brings its customers and suppliers together with the general managers of its many business units in strategy sessions aimed at creating new market opportunities. In each case, HP defines a "business ecosystem," the framework posed by GeoPartners' Moore, for its managers to explore and analyze. In an ecosystem, companies sometimes compete and often cooperate to come up with innovations, create new products, and serve customers. "Most of the business managers are so busy minding their current businesses that it's hard to step out and see threats or opportunities," says Srinivas Sukumar, director of strategic planning for HP Labs.

strategic intent n: A tangible corporate goal or destiny that represents a stretch for the organization. It also implies a point of view about the competitive position a company hopes to build over the coming decade

By looking at the entire ecosystem, it provides a broad perspective to them. It gets people out of their boxes."

A session on the ecosystem for the automotive industry saw HP assembling managers from divisions that make service-bay diagnostic systems for Ford Motor Co., workstations in automanufacturing plants, and electronic components for cars. The company also invited customers and suppliers. What could all these divisions do together to create new value for the industry? "Many of the opportunities came right out of the mouths of customers," says Susan Burnett, who heads executive development at HP. Possibilities: creating "smart" highway systems or building integrated systems that would collect service problems and immediately feed them back to Detroit. "It changes your vision of the business future," says Thomas E. Vos, general manager of HP's electronic-instruments group. "You start thinking about how you can get increased value from all the pieces of our company."

By inviting such a broad range of people to the strategy table, HP gained viewpoints that would normally not be heard. Yet those opinions are critical to creating future products and markets. "You have to bring in new voices to the process," says Hamel. "I find it amazing that young people who live closest to the future are the most disenfranchised in most strategy-creating exercises."

Electronic Data Systems Corp., which manages large-scale data centers, has opened its strategic-planning process to an even broader range of players. Four years ago, EDS

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THREE OF THE BUSIEST NEW STRATEGISTS



GARY HAMEL, *Strategos*

Of the new generation of strategy gurus, no one is in greater demand these days than Gary Hamel. Within the past 18 months, the lanky 41-year-old academic has delivered nearly 75 speeches and built a consulting company that is generating revenues of \$20 million a year.

Together with University of Michigan professor C. K. Prahalad, Hamel has redefined the world of corporate strategy. For decades, strategists spent much of their time figuring out how to position products and businesses within an industry. Instead, Hamel argues, strategy should be about changing industry rules or creating tomorrow's industries, much as Wal-Mart Stores Inc. did in retailing or Charles Schwab did in the brokerage and mutual-fund business.

Hamel urges managers to determine their company's "core competencies," or key corporate skills, and to create "strategic intent" based on these skills and the development of others to invent a new future. "Strategy has to be subversive," he declares. "If it's not challenging internal company rules or industry rules, it is not strategy."

Hamel also urges clients to "democratize" the strategy creation process. "It is imagination and not resources that is scarce," he says. "So we have to involve hundreds, if not thousands, of new voices in the strategy process if we want to increase the odds of seeing the future."

Hamel changed his own future in 1978 when he quit his job as a hospital administrator and went to the University of Michigan for a PhD in international business. At Michigan he met Prahalad. "We shared a deep dissatisfaction with the mechanistic way strategy was carried out," Hamel says. The pair wrote a series of influential essays published in the Harvard Business Review and put their ideas into a book, *Competing for the Future*, in late 1994. It has become gospel for managers around the world, many of whom now seek advice from Hamel's firm, Strategos Inc., in Menlo Park, Calif.

ADRIAN SLYWOTSKY, *Corporate Decisions*

Like other strategic-planning gurus start with the capabilities and skills of a company, Adrian J. Slywotsky begins with customers. A founding partner of Boston-based Corporate Decisions Inc., Slywotsky maintains that too much of corporate strategy has been based on a mindset that failed to understand what customers want and need.

He urges managers to begin the strategy process by recognizing where stock-market value is migrating in an industry. Shifts in value—for example, from Sears, Roebuck & Co. to Wal-Mart Stores Inc.—usually reflect shifting customer priorities. By falling out of touch with those needs, one U.S. company after another has lost ground to new, aggressive rivals. Companies such as Microsoft, Nucor, and Intel have captured growth and stock market value by doing what Slywotsky says are “superior business decisions”—configuring resources and going to market based on a deep understanding of customers’ priorities. “Strategy is not making choices,” says the 45-year-old consultant. “Do you have this customer group or a different one? How are your customers and prospects changing? If my business model was good for yesterday’s customers, how does it need to change to keep them?”

A Harvard-trained lawyer, Slywotsky returned to the university for his MBA in 1978. After a three-year stint as consultant Bain & Co., he founded Corporate Decisions in 1983. His novel views of strategy, detailed in his book *Value Migration*, have won audiences at such major companies as Sears, Philips Electronics, and Searle Pharmaceuticals.

Slywotsky’s corporate fans find much appeal in his notion that strategy has paid far too much attention to simple gains in market share. By instead examining the business models that are capturing stock-market value, Slywotsky says managers can find templates for changes within their organizations.



JAMES MOORE, *GeoPartners Research*

James F. Moore, founder and chairman of Cambridge-based GeoPartners Research Inc., is an unlikely corporate strategist. For one thing, his PhD is in cognitive psychology. For another, he once taught art and photography in a New Haven high school—hardly typical training for any would-be counselor to Corporate America.

But with the recent publication of *The Death of Competition*, the 47-year-old Moore has quickly distinguished himself as an original thinker and hot New Age strategist. Moore relies heavily on metaphors from biology and ecology to help managers better understand the dynamics of competition and create successful strategy.

He urges clients at such companies as AT&T, ABB Asea Brown Boveri, Royal Dutch/Shell Group, and Hewlett-Packard to view themselves as part of a “business ecosystem.” Why? “The new paradigm requires thinking in terms of whole systems,” he says. “Seeing your business as part of a wider environment.”

That demands viewing business opportunities not simply from the perspective of a solo player but as one player among many, each “co-evolving” with the others. That’s sharply different from the conventional idea of competition, in which companies work only with their own resources and do not extend themselves using the capabilities of others.

Among other things, Moore favors seeking out partners to create something of value, achieve market coverage, and block alternative ecosystems. In later stages of the business ecosystem, members must look beyond their community for new ideas and work to prevent partners and customers from defecting. And all the while, he says, companies must reach out to customers to predict how marketplace changes may occur. “The major challenge for many companies is to get others to co-evolve with their vision of the future,” says Moore. “In a global market, you want to make use of the other players—for capacity, innovation, and capital.” In the corporate Galapagos, it’s co-evolve—or die.

By John A. Byrne in New York

launched a major strategy initiative that involved 2,500 of its 55,000 employees. Using Hamel to help guide the process, the company picked a core group of 150 staffers from around the world for the yearlong assignment. The group ranged from a 26-year-old systems engineer who had been with EDS for two years to a sixtysomething corporate vice-president with a quarter of a century of EDS experience. Similar approaches have been used by a wide range of companies, including Marriott Hotels and Helene Curtis Industries.

POINT OF VIEW. At EDS, staffers identified potential "discontinuities" that could threaten or pose opportunities for EDS. They isolated the company's core competencies—what it does best and how that differentiates it from the competition. And they crafted a "strategic intent"—a point of view about its future. "We discovered that in order for us to make information technology valuable to people, we had to be able to go into a company" and offer consulting to provide more complete solutions, says Rick Barretta, a corporate vice-president. "You couldn't do that without building a business strategy." So EDS began to create a management-consulting practice, acquiring

Cover Story

A. T. Kearney Inc. last year for \$600 million.

J. M. Smucker Co., the Ohio-based maker of jams and jellies, more recently enlisted a team of 140 employees—7% of its workforce—who devoted nearly 50% of their time to a major strategy exercise for more than six months. "Instead of having just 12 minds working it, we really used the team of 140 as ambassadors to solicit input from all 2,000 employees," says President Richard K. Smucker. "It gave us a broader perspective, and it brought to the surface a lot of people with special talents." The company, which has struggled to grow in a mature market, now has a dozen viable initiatives that could double its \$635 million revenues over the next five years. One of them is a just-announced alliance with Brach & Brock Confections Inc. to make Smucker's jellybeans, the first of several co-branded products to be developed under the pact. The idea came from a team that included staffers who ordinarily would never have had a role in strategy formulation.

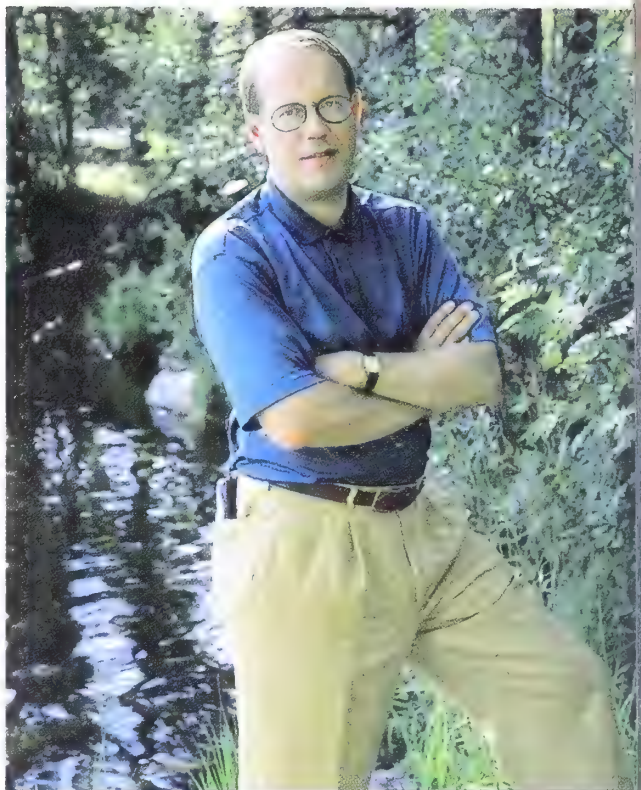
business eco·sys·tem n: System in which companies work cooperatively and competitively to support new products, satisfy customers, and create the next round of innovation in key market segments

Unlike slow-growing Smucker's, Finland's Nokia Group had been exploding at a rate of 70% a year in the booming telecommunications business when it chose to involve 250 employees in a strategic review early last year. "By engaging more people, the ability to implement strategy becomes more viable," says Chris Jackson, head of strategy development at Nokia. "We won a high degree of commitment by the process, and we ended up with lots of options we hadn't looked at in the past."

Among other things, the review forced managers to look at the convergence of different technologies and how they would

"The smart-car project needed a multitude of disciplines to master the solution"

JORMA OLLILA
CEO, Nokia Group



affect the company. The most tangible benefit to date is the creation earlier this year of a new "smart-car" unit in Germany to develop products for the auto industry. Nokia hopes to use its expertise in cellular networks to create such products as integrated navigation and road-guidance systems. "The smart-car project needed a multitude of disciplines to master the solution that will win in the future," says CEO Jorma Ollila. "The think-tank approach addressed this challenge effectively."

The company's top executive team now meets monthly with a strategy agenda. Nokia also says that the line managers who spent a quarter of their time over six months on the exercise now have the training and perspective to make strategy a regular part of their jobs. "We've taken strategy away from the yearly cycle that it was in, and we're trying to make it a daily part of a manager's activity," says Jackson. "We haven't quite arrived at that yet, but we're clearly moving in that direction."

SUMMER BRAINSTORMS. That's also the direction Jack Welch has been moving in ever since he nuked GE's central-planning department. Welch pushed responsibility for strategy down to each of General Electric Co.'s 12 unit heads, who meet every summer with Welch and his top management team for day-long planning sessions. "The focus is on strategy, both near-term and a four-year look into the future," says Steven Kerr, vice-president for corporate management development. "They lay out what they are going to do, what new products they are interested in, and what our competition is doing." The Corporate Executive Council, a group of GE's top 24 execs, also meets four times a year to dissect each business and where it is headed.

But there's no one at GE with the title of head of strategic planning. "If you had one, what would such a person do?" asks Kerr. "He would require reports." Bound in vinyl, no doubt. Definitely not the way the strategic-planning game is played anymore.

By John A. Byrne in New York, with bureau report

EDITED BY OTIS PORT

SURFING ON SHOCK WAVES

AVIATION ENTHUSIASTS attending the Experimental Aircraft Assn. show in Oshkosh, Wis., earlier this month got a special treat: NASA and the Air Force rolled out a model of the futuristic LoFlyte Mach 5 Waverider. This is the first plane designed to go five times the speed of sound and survive the extreme stress of a hypersonic shock wave—by actually riding on top of the wave. By comparison, the current speed



champ—the Lockheed SR-71 Blackbird—tops out at just over Mach 3, or 2,194 mph.

The current Waverider is only an eight-foot-long, remote-controlled model, and it won't even attempt to set any new records. Instead, it

will be used to determine whether an aircraft designed to skip along atop a hypersonic shock wave is also stable enough at low speeds to take off and land safely.

NASA will begin the testing in a couple of weeks. If all goes well, a 23-foot pilot-ed prototype will be next.

Because the Waverider will be tricky to fly, the pilot will need the help of a

“smart” control system, and Accurate Automation Corp. in Chattanooga, Tenn., has developed one that uses neural networks. By emulating primitive brain circuits, neural networks learn from experience. The system will handle “upsets” that require instant correction—

things no human could react to quickly enough. Mississippi State University's Raspet Flight Research Laboratory built the airframe, and SWB Turbines in Appleton, Wis., supplied the jet engine.

THE FLAG IS UP IN YOUR MAILBOX

OFFICE WORKERS ON LOCAL-area networks usually get giddy when E-mail arrives. But people working at home aren't so lucky. To find out if there's a new item in their mailboxes, they typically have to fire up a modem or have a phone line continuously open.

Next month, there will be a new option: AirMedia Live from Ex Machina, a software house in New York. Working with CompuServe Inc. and various Internet suppliers, AirMedia will broadcast news alerts to small receivers plugged into PCs. Arriving news flashes—from real-time stock quotes to sports scores to headlines from Reuters—will cause icons to pop up on the screen.

Narrow-band wireless

transmissions can't carry a great deal of information. But the icons will work like the ones found on the World Wide Web. Click on one and the computer will dial into the Internet and go to the appropriate site.

AirMedia is planning to give away basic services, including market updates, while charging about \$5 a month for a basket of others. Receivers will run about \$150.

Neil Gross

THIS GIZMO SIZES UP DRUGS BY THEIR GLOW

THE CHORE OF SEARCHING for new medicines has just gotten easier. A new instrument called Discovery, from Packard Instrument Co. in Meriden, Conn., can screen 50,000 potential drugs a day—five times more than existing technology. The system, which is the size of two file drawers, does not require the radioactive isotopes that are now widely used.

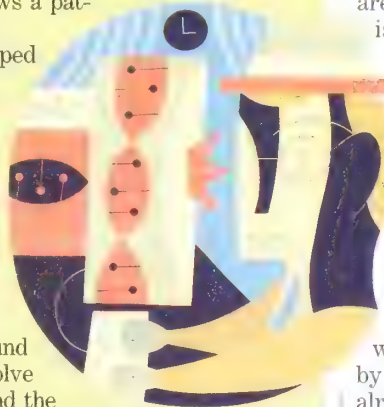
Candidate drug molecules are currently coated with an isotope, and any interaction with a target pathogen or molecule is signaled by minute changes in radioactivity. But Packard's Discovery tool uses phosphorescent chemicals patented by CIS, a French biotech company. A positive effect immediately shows up as a glow, which cuts screening time by 80% or more. Packard has already sold units to a few drugmakers, including Bristol-Myers Squibb, Rhône-Poulenc, and Zeneca Pharmaceuticals. Susan Jackson

A DNA 'SOFTWARE' SHORTCUT

TWO YEARS AGO, COMPUTER SCIENTISTS thought there might be a totally new way to build tomorrow's number-crunchers: Instead of transistors, use DNA molecules, which are far smaller. Leonard Adleman of the University of Southern California actually solved a simple problem by growing the answer in DNA. Enthusiasm waned, however, when scientists determined that solving tough problems would take oceans of DNA. That's because DNA computing is very wasteful.

For example, data is digitized by using a scheme based on chemical sequences within DNA strands. Since scientists don't now have a good way to custom-make strands of DNA, they have to grow them with all of the possible combinations, then select from among millions of strands those that contain the correct sequences.

Now, Mitsunori Ogihara of the University of Rochester believes he has devised an algorithm that might avoid most wasted steps. It borrows a pattern-matching process, developed for artificial-intelligence research, that should quickly shut down the growth of useless families of strands. If his approach does work, Ogihara figures one pound of DNA could solve problems beyond the scope of all the world's supercomputers. He hopes to prove it with a simulated DNA computer before yearend.



DEALS

MIKE MILKEN SWINGS —AND MISSES

He and a few big-name pals are getting burned at ICS Communications

In 1990, Michael R. Milken pleaded guilty to six felony counts of securities law violations. He paid more than \$1 billion in fines and restitution and was banned from the securities industry for life. After serving two years in jail, he is still waiting for his probation period to end, in late October.

With such a past, Milken can't be doing much wheeling and dealing, right? Wrong. The former junk-bond kingpin still has a knack for putting together deals with his old circle of friends. But what is missing—in one instance at least—is the old Milken knack for picking winners.

The loser is ICS Communications Inc., a small, private Dallas-based company that provides apartment dwellers with cable-TV and phone ser-



MERV ADELSON
The original backer of ICS, this former movie mogul helped launch ICS and brought in Milken, his former banker.

vice. All in all, \$200 million has been poured into ICS, says Steiner. "The performance [of ICS] has been terrible." Mervyn L. Adelson, who helped launch ICS, agrees: "Everybody involved underestimated the amount of capital it would need in order to provide what the clients wanted."

Milken's spokesman, Michael Reese, says Milken is spending most of his free time working on efforts to find a cure for prostate cancer, from which he suffers. He "remains a passive

though interested investor" in ICS. Reese confirms that Milken lost money in ICS but won't say how much.

The ICS saga began in 1993 when Merv Adelson's sons, Hollywood producers Andrew and Gary, bought Casden Cable, a Los Angeles cable-TV service, and renamed it ICS Communications. Adelson,

the former head of Lorimar Telepictures, interested Milken in the company in February, 1994. Milken would eventually invest about \$25 million, according to sources familiar with the deal. Reese, however, says Milken invested far less than \$25 million in ICS and mostly in the form of a loan. The company provided cable-TV service to about 4,000 households and had about 35 employees.

At the time, the market for what is called shared



JEFFREY STEINER
SHARED TECHNOLOGIES
His company, Shared Technologies Fairchild, inked a deal this June to manage ICS.

A MILKEN REUNION

The former junk-bond king and his ex-Drexel clients have invested in a small Dallas company, ICS Communications. Some \$200 million later, ICS is floundering.



MICHAEL MILKEN
He invested about \$25 million in ICS Communications.

tenant services was in its early days. The idea was for ICS to sign contracts with apartment building owners to provide all of the tenants in their buildings with cable-TV

and phone service. ICS would then install satellite dishes on the roofs, wire the buildings, and provide an array of services, from television channels just for building news to electronic security. "It was a

great-sounding idea. If you hook up the landlord, you control distribution to the building," says one banker. "Milken was very excited about the prospects."

But fairly quickly, ICS began to veer off course. I



MAX CHAPMAN
NOMURA
Nomura Securities at ICS Communications \$77 million. The loan is now being restructured.

Technologies Fairchild Inc. was brought in to manage ICS. That company's vice-chairman, Jeffrey J. Steiner, was a big beneficiary of Milken's junk-bond ma-

mushroomed to 250 employees and 100,000 subscribers, with about \$35 billion in revenues. Instead zeroing in on a small number of cities and concentrating on providing old service, it bought a company called MaxTel and expanded its operations to states in an effort to go national. Spread so thin, it couldn't even bill its customers for services rendered. "They made a huge number of commitments and simply weren't able to construct systems they promised to build," says John Mansell, senior analyst at Kagan & Co. Says Kevin Schott-

under, the Shared Technologies executive who is now running ICS: "I don't disagree that they grew too damn fast. I hope to prove to our clients that we're serious about customer service and putting these issues behind us." Milken then recommended Spiegel to Adelson and Spiegel was hired as a management consultant and a director, confirms Reese. Spiegel ran Columbia Savings & Loan, which bought billions of Drexel junk

bonds, and was acquitted of charges of looting the Beverly Hills thrift. He worked two months as a consultant yet is still a director. Spiegel did not return calls. By yearend 1994, ICS expended money badly. Milken introduced MCI and News Corp. to ICS and they became the largest investors," says a banker with knowledge of the deal. MCI and News Corp. had ponied up \$30 million, 7 former ICS employees and bankers. Milken had been close to MCI since 1983, when Drexel Burnham Lambert Inc. raised \$1 billion for MCI. In 1995, Milken advised MCI on its \$1 billion investment in News Corp. Frank Walter, MCI spokesman, didn't respond to questions and minimized MCI's involvement with ICS. "We're a



RUPERT MURDOCH
NEWS CORP.

News Corp., a current Milken client, invested \$30 million in ICS in 1995. It is the second-largest investor.

knew Rupert Murdoch. "I brought them in. Mike may have provided an introduction, but he had nothing to do with the negotiations." News Corp. would only confirm that it has a minority stake in ICS.

Milken denies he solicited money from MCI, News Corp., or any other investor, nor did he play a manage-

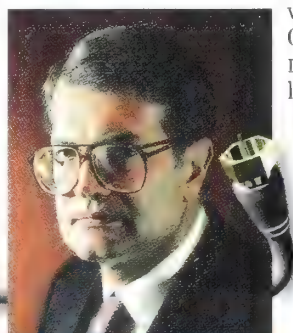
ment role in ICS. "He never exercised control or attempted to exercise control by imposing individuals into management positions and has never been paid a fee by MCI or ICS of any kind," says Reese.

Milken did take more than a passing interest in his investment. "We had periodic meetings with him," says David Burdge, a former ICS senior vice-president.

Yet for Milken, the issue of who raised funds for ICS and whether he received a fee is the crucial one. For his probation to end, the Securities & Exchange Commission has to conclude its investigation into his role in three transactions. At issue is whether Milken is adhering to his lifetime ban from the securities industry. The ban requires that Milken not be "engaged in the business of effecting transactions in securities for the accounts of others," says John J. Coffee Jr., a securities law professor at Columbia law

minority investor," insists Walter.

Adelson says he approached MCI on behalf of ICS, not Milken. However, Adelson credits Milken with introducing him to MCI's Bert C. Roberts Jr. at a charity dinner in Los Angeles. Roberts was seated next to Adelson and Milken and their respective spouses. Milken introduced the two men and mentioned his investment in ICS. "I did the negotiations with MCI," says Adelson. Adelson says he also approached News Corp. and that he already



THOMAS SPIEGEL
BRANTROCK GROUP

Recommended by Milken, he became an ICS director and manager in 1995. He's still a director.

school. It's O.K. if as an investor, he is just helping his company get financing, says Coffee. But "add a fee to it and it's something that could cause a problem," says Coffee.

By fall, 1995, MCI realized it had to take direct action to rescue its investment. MCI replaced Andrew and Gary Adelson, who were co-chairmen, with a CEO from MCI. The offices moved to Dallas from Los Angeles. Andrew and Gary Adelson declined comment.

ICS was still hemorrhaging cash. Enter Nomura Securities International Inc. and its chairman, Max Chapman, who had just met Milken for the first time at a Nomura real estate conference in Arizona. Despite the poor condition of the company, Nomura granted a \$77 million bridge loan. Some \$29 million went to MCI and \$5 million more went to Milken to repay their loans to ICS,

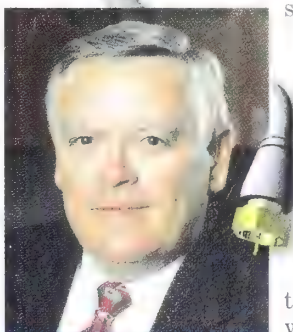
with \$17 million to MaxTel. Only \$26 million went to ICS. Eight days later, the loan went into technical default—it failed to meet its loan covenants because it missed certain financial ratios. Nomura spokesman P.J. Johnson says the firm "does not comment on current deals or proprietary investments."

KEY HELP. In June, MCI announced a joint venture with Shared Technologies to run ICS. Its vice-chairman, Steiner, says he spoke to Milken on the phone about the deal and that Milken was "quite happy Shared Technologies is taking over management." Steiner says the deal jelled after talks between Adelson and Anthony D. Autorino, the CEO of Shared Technologies, and then conversations between Autorino and MCI.

Nomura and MCI are trying to restructure the bridge loan. One key executive involved in that loan, Robert D. Long, resigned in July over what insiders say are differences of opinion over how the bridge-loan business should be run. Right now, ICS is losing big money. In recent weeks, MCI has been putting about \$1.5 million a week into ICS to keep it going, say sources close to the deal. Nomura could see losses of \$25 million, say sources close to the company. As for Milken, he is still about \$20 million in the hole.

It's possible that the new management at ICS can turn the company around. But even if that happens, the ICS deal will not go down as one of Milken's shining plays.

By Leah Nahans Spiro in New York



BERT ROBERTS
MCI

MCI Communications, a longtime Milken client, poured over \$100 million into ICS since early 1995.

BANKING

CLIPPING THE WINGS OF CREDIT UNIONS?

A U.S. court ruling could bar nonemployee members

Mike Parleir needed only \$5,000 more for a downpayment on a house in Asheboro, N.C., two years ago. But none of the area banks would touch him, even though his \$50,000 salary from a food distributor was high by local standards. The reason: Parleir's own seafood eatery had ended up in bankruptcy in 1992. So Parleir turned instead to the credit union available through his employer—the AT&T Family Federal Credit Union based in nearby Winston-Salem. "I'm pretty loyal to them," says Parleir. "When I needed help, they were the only ones who came to my defense."

But Parleir's love affair with his credit union could be in jeopardy. On July 30, a federal appeals court in Washington delivered a potentially harsh blow to AT&T Family Federal Credit Union and thousands of similar institutions. In a precedent-setting decision, a three-judge panel ruled that regulators had improperly allowed credit unions, formed to serve specific employee groups, to add members from unrelated companies or professions.

The full impact of the decision won't be known until a lower court fleshes out new rules for the industry, which won't occur before October. But at the least, legal experts believe occupation-based credit unions such as AT&T Family may be barred from accepting new members from outside their core employee groups. At worst, the lower court could force the institutions to divest millions of non-employee members such as Parleir—essentially breaking up roughly 2,000 of the largest credit unions. The ruling "has the potential to be catastrophic," worries Robert M. Fenner, general counsel to the National Credit Union Administration, the regulator chastised by the court.

CHERRY-PICKING? The tremendous expansion of credit unions began in 1982. At the time, NCUA officials realized that the recession driving many old-line manufacturers out of business was in turn causing their credit unions to fail



REJECTED: Millions may lose their privileges

as laid-off employees were unable to pay off credit-union loans. Massive failures would have forced the government to bail out depositors at taxpayer expense. So the NCUA allowed credit unions to diversify their memberships beyond their own companies, organizations, or communities.

The policy change touched off a boom. Since 1982, credit unions have grown

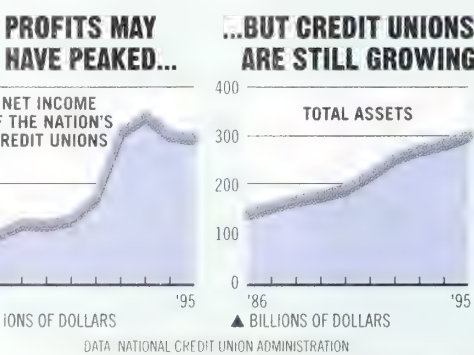
roughly fourfold, controlling at midyear an estimated \$330 billion in assets from about 70 million members. Much of the growth has come from luring customers from outside: Only one-third of AT&T Family Federal's members actually work for the phone giant. Instead, most of its \$480 million in assets come from nearly 300 other organizations stretching from Ohio to Florida.

Not surprisingly, bankers are furious about losing customers. They gripe that the credit unions' nonprofit status—which frees them from paying income taxes and shareholder dividends—gives them an unfair pricing advantage. The credit unions say the differences reflect the better credit risks of its members, among other factors. But bankers argue that credit unions have strayed too far from the original mission as Depression-era cooperatives, lending to workers denied credit by banks, and are increasingly catering to the white-collar crowd. "They come in and cherry-pick the most profitable business and then give nothing back to the community," complains Joe G. Howard, senior vice-president at First National Bank & Trust Co. in Asheboro, N.C.

APPEALS PROCESS. In 1989, First National, four other North Carolina banks, and the American Bankers Assn. sued the NCUA for allowing AT&T Family Federal's heady expansion. They argue that NCUA's move violated a 1980 law establishing federal credit unions. After years of legal wrangling, the appeals court agreed, ruling that "all members of a [credit union] must share a common bond."

Credit unions plan to take their fight to the U.S. Supreme Court. If they don't win, they vow to ask Congress for relief. They note that all credit unions combined are still only about the same size as the U.S.'s largest commercial banking company, Chase Manhattan Corp. They also contend that bankers' woes stem mostly from poor treatment of depositors and borrowers. "Banks should expend their energy on improving their customer service rather than trying to pull apart credit unions," says AT&T Family Federal President Marc Schaefer. But if the appeals court ruling stands, people like Mike Parleir could be back out on the street looking for a friendly lender.

By Dean Foust in Washington



By Michael Schroeder

NASD-Y HABITS WILL HAVE TO CHANGE

Barely a peep has come out of the National Association of Securities Dealers since it was censured on Aug. 8 for failing to halt widespread price-fixing of stocks on its NASDAQ market. In a settlement negotiated over two months, the NASD agreed to spend at least \$100 million during the next five years to upgrade policing efforts, to develop an audit system for tracing every stock transaction, and to improve surveillance. The unprecedented action against the world's second-largest stock market should correct the unfair advantage brokerage firms have held over investors for years.

Why is the NASD so quiet? It's out of character for an organization that fought the Securities & Exchange Commission at every turn during the 18-month investigation. But the association knew better than to bad-mouth the settlement. Says an SEC official: "We told them, 'If you deny the allegations, you do so at your peril.'"

Now that the SEC probe has concluded with a pact highly critical of the over-the-counter market, the question remains: Will the NASD voluntarily embark on the road to real reform? If its record is a guide, the answer is no.

CHEERLEADER. The settlement is no act of repentance. Indeed, the two top executives, Joseph R. Hardiman and Richard G. Ketchum, have never acknowledged serious market flaws. This denial persisted in the face of SEC evidence of an NASD "culture" that tolerated trading violations. SEC negotiators were stunned that a week before the pact, Ketchum was disputing the issue at the heart of the probe: the existence of a "pricing convention" in which brokers colluded to keep bid and ask prices artificially wide to line their pockets at investors' expense. Even Wall Street brokerages had confirmed to the SEC an ingrained system for keeping spreads wide.

What's most disturbing is that the NASD was aware of burgeoning prob-

lems as far back as 1990 but did nothing. Settlement documents depict an organization that neglected its oversight responsibility and became a cheerleader for its NASDAQ stock market.

When the trading abuses came to light in 1994, the NASD viewed them as a public-relations problem rather than a call for self-examination. One reason: The NASD was dominated by a few dozen firms—among them



SEC CHIEF LEVITT COMPLAINS OF FOOT-DRAGGING

Inside the NASD, there are worries that NASDAQ companies will start jumping to the Big Board

Merrill Lynch, Smith Barney, and Dean Witter—whose self-interest was the status quo. When NASDAQ continued to boom, the NASD took it as an endorsement from its customers.

At a time when the NASD should have been spending more money to police its 5,400 member firms, its 1994 annual report trumpeted a bigger advertising budget to "broaden NASDAQ's market recognition and trust." Money also was spent on studies to refute criticism. In the settlement, the SEC refers to one unusual arrangement with an economist: If the NASD didn't like the results of a commissioned study on trading costs, it would pay an extra \$1,000 to prevent publication.

Public relations permeated every effort, including a 1994 committee headed by former Senator Warren B. Rudman (R-N.H.), to propose organizational changes. The NASD agreed to adopt most of the Rudman group's recommendations to overhaul the NASD's structure. The SEC fumed that the NASD expected cosmetic changes to put an end to the SEC probe. To its credit, the SEC resisted huge lobbying from Wall Street firms.

SKEPTICAL. To the end, the NASD failed to come clean about its problems. In early June, the SEC sent the association a draft settlement. But the NASD continued to oppose the inevitable censure and publication of details of NASDAQ trading violations. The lawyers argued that the SEC would undermine confidence in the market and hurt liquidity of the stocks that trade there.

NASD member firms still are facing a class action. Their lawyers worry that admitting any trading violations could end up as part of the court case. But the silence strategy has backfired, resulting in a steady drumbeat of bad press. Inside the NASD, there are worries that the larger NASDAQ companies will start jumping to the New York Stock Exchange.

Much of the pain could have been avoided had the NASD been more cooperative. The whole matter "should have been resolved a long time ago," says SEC Chairman Arthur Levitt Jr.

The commission is skeptical the NASD will move fast and far enough. The agreement calls for the association to hire an independent consultant to report back to the regulator on compliance. But the commission should be wary that the NASD doesn't hog-tie the consultant, much as it did the Rudman committee. The SEC should keep an eagle eye on the market to make sure the reforms aren't just another public-relations ploy.

*Washington Correspondent
Schroeder covers securities regulation.*

BY GENE G. MARCIAL

DUPONT'S DIET MAY NOT BE OVER

DuPont (DD) has been shedding fat fast. It slashed costs by \$3 billion in the past four years and raised labor productivity by 3% a year, according to analysts. But some investment pros are betting DuPont will do much more to please investors who think the stock, now at 82, merits a higher price. Paul Raman, an analyst at PaineWebber, insists that DuPont will sell some important assets.

"DuPont's repurchase of shares held by Seagram was the catalyst for the big future change," says Raman. In April, 1995, DuPont paid \$8.8 billion to buy back 156 million shares from Seagram. And last July, DuPont bought back warrants for DuPont stock that Seagram also held, for \$500 million.

Raman is betting that DuPont CEO Jack Krol "has a scheme in mind—one that could make the stock go as

high as 95 to 100," Krol, he believes, will opt to sell Conoco—which DuPont acquired in 1981—for \$12 billion to \$14 billion, or \$20 to \$22 per share in DuPont stock. Conoco has \$800 million in aftertax income and \$2.1 billion in aftertax cash flow, notes Raman.

The analyst says that DuPont will use the cash to pay down debt, repurchase a huge number of shares, and bolster its key businesses overseas, including nylon, agrichemicals, titanium oxide, and specialty fibers.

"I expect DuPont will also shed its imaging and coal businesses," says Raman. The imaging business (films and printing systems), he notes, generates sales of about \$800 million a year. He believes the operations will be bought by Xerox or Fuji Photo Film of Japan for about \$700 million.

DuPont's 50% stake in the coal business (co-owned with Consolidated Energy) produces operating income of \$90 million and may end up with a

German energy company for about \$1 billion, says Raman. A DuPont spokeswoman says the company has a policy not to comment on speculation.

IS GATORADE FOR SALE?

The stock of Quaker Oats (OAT) has been a terrible laggard, but CEO William Smithburg vowed in late July that he would "move every mountain," to boost its value. Well, one of the mountains to be moved, whispers the chief investment strategist at a New York investment bank, is Gatorade. With sales of \$1.2 billion last year, Quaker's Gatorade unit is estimated to be worth \$3 billion, or about 23 a share. In 1995, Quaker had sales of \$6.3 billion.

According to this banker, a large beverage company has expressed interest in Gatorade to complement its own sports-drink product. In that go-go market, Gatorade is believed to control 80% of sales. Coca-Cola's Powerade and PepsiCo's Allsport are the two other U.S. products in that category.

Quaker has hired a Wall Street law firm and an investment bank to lay the groundwork for the sale, according to the banker. Unloading Gatorade, he adds, is the first move in a series of steps in restructuring Quaker to enhance shareholder value. "Smithburg is dead serious in seizing this opportunity to shake up the company," he says.

Quaker stock has been stuck in the 30s: On Aug. 13, it closed at 31, down from its 52-week high of 37%. Two years ago, it was trading at 43. Based on its breakup value, says one analyst, Quaker is worth 48 to 50 a share.

Earlier rumors were that Quaker would sell Snapple—acquired in December, 1994, for \$1.7 billion—because of poor sales. Quaker may still sell off Snapple, along with Gatorade, the banker says. In the second quarter, sales of Snapple, which produces ready-to-drink tea and fruit drinks, fell 10% behind year-ago results. Quaker has integrated Snapple with Gatorade operations.

Lately, Quaker has also been haunted by disappointing sales in its ready-to-eat cereals, with volume dropping 7% in the second quarter. The drag in sales has prompted a cut in prices. Spokesman Ron Bottrell says that the company doesn't comment on market speculation.

UROHEALTH LOOKS MORE ROBUST

UROHEALTH Systems (URO) has been in a whirlwind of buyouts. The maker of urological and gynecological devices has snapped up companies in an effort to become a one-stop shopping outlet for such gear—four acquisitions this year on top of five last year.

So far, the strategy has worked. In

IT'S DRAWING BIG INVESTORS



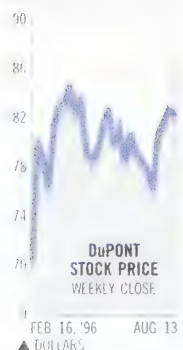
the past two quarters, UROHEALTH has changed from a loss-ridden operation into a moneymaker. And the company has attracted savvy players: A group including Leon Black, who heads Apollo Advisor, acquired a 22% stake. Apollo invested \$22 million through the purchase of securities and debt. "We're impressed with the company's growth-and-acquisition strategy," says Mike Gross, a partner at Apollo.

David Pyrcce, of San Francisco's investment firm Van Kasper, figures the shares, now at 12¢ are worth 20. He sees the company making 61¢ a share on revenues of \$81.6 million and sees revenues rising to \$120 million in fiscal 1998 and per-share earnings to \$1.10.

Pyrcce's 1997 and 1998 earnings estimates, he explains, do not include the benefits from UROHEALTH's most recent acquisition: Richard-Allen Medical Industries, a maker of products for the gynecological and general-surgery markets, with annual sales of \$21 million. He figures the newcomer will boost revenues to around \$100 million and add 10¢ a share to the bottom line.

Pyrcce notes that CEO Charles Laverty is "highly shareholder-oriented" and is building up UROHEALTH's assets and product line to create a company that larger outfits may be interested in. "I wouldn't be surprised if it ends up a takeover target itself," says Pyrcce.

BUYBACKS COULD UP THE PRICE



Source: Bloomberg Financial Markets, Van Kasper & Co.

BALLOT INITIATIVE

POWER POLITICS— IN SILICON VALLEY?

High tech gears up to fight off the tort lawyers

It's barely sunrise on Aug. 9, and the titans of technology are filing into a meeting in the heart of Silicon Valley. On hours' notice, Hewlett-Packard CEO David P. Patil, Intel chairman Gordon E. Moore, and Apple CEO Steve Jobs join 45 other leaders from companies representing more than \$370 billion in market value to tackle what they say is a life-threatening issue. What has woken them from bed early? A ballot initiative that, if passed this fall, would make it easier for investors to sue companies whose stock price drops sharply. And directors and officers could not be indemnified if they are found to have contributed to the wrongdoing. "It's like a neutron bomb going off in the boardroom," says Steven P. Jobs, CEO of Pixar Inc. "There will be no one left in the chairs."

ARMED WAGONS. Such emotion from the top and others isn't surprising. The volatile technology sector is especially vulnerable to claims of stock fraud. What is new is the sleek lobbying machine emerging in an industry that had previously been politically inept. For the first time, the high-tech community is rallying its considerable resources to form an organized—and professional—opposition. The momentum is giving Silicon Valley to establish a permanent bipartisan out-let called the California Technology Alliance, to address concerns ranging from trade issues to capital-gains taxes. "Until now, high-tech, high-growth companies haven't been involved in government," says venture capitalist L. John Doerr, host of the dawn powwow. "That has changed forever."



POLITICAL MACHINE SHOP: Defeating 211 is only a start

What's rousing the insular community is the realization that Silicon Valley's political muscle isn't nearly as impressive as its economic might. Now technology companies are being drawn together by a common threat: a ballot proposal known as Proposition 211 that would turn California into a haven for securities suits. A handful of small companies, such as San Jose chipmaker Monolithic System Technology Inc., has even vowed to abandon the state if the measure passes. Many directors of public companies are threatening to resign.

Proponents of Prop. 211, who include a nationwide coalition of plaintiffs' lawyers and consumer groups, argue

that federal law reform passed last year makes it too hard for ripped-off shareholders to recover their money. By making it easier for investors to sue companies that exaggerate their prospects, the state initiative, they contend, will protect small investors and ensure healthier markets. "Corporate America knows that if it beats us, then it is home free to do anything it wants," says plaintiffs' attorney Melvyn I. Weiss.

The last time Silicon Valley and trial lawyers squared off was in March, when the industry launched three initiatives aimed at curbing litigation. But it raised money too late to bring its message to the voters, and the measures failed. Not this time. By June, nearly \$7 million had been collected. Even non-California companies such as Compaq Computer Corp., feeling threatened by 211's possible effects on their directors and bottom line, are chipping in. "Having learned the hard way, we've gotten people on fire about this," says Intuit Inc. co-

founder Tom Proulx, who ran the March campaign.

Apart from better fund-raising, this campaign is better managed. Ads began running three days before the proposition was even assigned a number. When it got the 211 label, the campaign was ready to go, since it had already shot five separate TV spots using five different numbers. In July, organizers recruited John A. Young, former CEO of Hewlett-Packard Co., to carry technology's message coast to coast. Playing to its strengths, Silicon Valley is also launching a sophisticated cybercampaign, linking its campaign Web site to internal networks of many companies.

A big payoff came on Aug. 7, when Clinton shocked his handlers—and trial lawyers—by opposing Prop. 211. Silicon Valley hopes it's just the beginning. "We will emerge from this campaign as an industry with a lot of political presence," says Proulx. Ironically, it plans to do that by mirroring its archrivals: the tort lawyers.

By Linda Himelstein in Menlo Park, Calif.

What Prop. 211 Would Do

Plaintiffs would not have to prove they were even aware of the allegedly fraudulent information

Accountants, brokers, and others who merely assisted in unscrupulous behavior could be sued by investors

Companies could not indemnify directors or officers personally responsible for corporate misconduct

DATA BUSINESS WEEK

THE TRIUMPH OF A QUIET MAN IN A NOISY BUSINESS

Tenacious Peter Georgescu has made Young & Rubicam Advertising a hot shop again

When the Iron Curtain came down on Romania in 1947, 8-year-old Peter Georgescu was sitting in a classroom in Bucharest. His father, Valeriu, an executive at Standard Oil, was at a business meeting in Rockefeller Plaza. Branded a capitalist enemy of the socialist state, the elder Georgescu, along with his wife, was barred from their homeland. Peter, his 13-year-old brother, Constantin, and their grandmother were put under house arrest. For 12 hours a day, six days a week, the boys dug holes and cleaned sewers.

They didn't see their parents again for seven years. Asked to spy for Romania to earn his sons' release, Valeriu went to the FBI. Ultimately, President Dwight D. Eisenhower intervened to win the boys' freedom. Arriving in the U.S. in the spring of 1954, they were hailed as anticommunist heroes. Their photo ran on front pages. Within two weeks, they threw out the first pitch on opening day at Brooklyn's Ebbets Field and appeared, with a translator, on *The Today Show* and *The Ed Sullivan Show*. "Ludicrous. Unimaginable," says Georgescu, still at a loss to describe his transformation from prisoner into icon.

It is perhaps fitting that today, more than four decades after becoming a cold-war hero, Peter A. Georgescu sits in a nerve center of free-market capitalism: the corner office at Young & Rubicam Inc., owner of Young & Rubicam Worldwide Advertising, one of the biggest agencies in the world. "This is still a war," he says, laughing at his own comparison. "An economic war."

GRIT. Georgescu, 57, has brought the same quiet intensity to his career that he once applied to remaking himself from a boy without education into a varsity soccer player majoring in political science at Princeton University. Named CEO of Y&R in January, 1994, and chairman a year later, Georgescu has turned the ad agency, which had been losing ground for years, into one of Madison Avenue's hot shops. And on Aug. 12, he broke a



COLD-WAR HERO: In advertising, it's "still a war. An economic war"

73-year tradition with the announcement that closely held Y&R Inc. was selling a minority stake to an outsider.

Georgescu seems to have barely paused for breath since Apr. 13, 1954, when he and Constantin touched down at New York's Idlewild Airport. By summer, he was at a camp in Maine, learning English. By fall, he was at New England's patrician Phillips Exeter Academy, where the headmaster admitted him after reading about him in the papers.

By his own choice, Georgescu entered 10th grade with others his age. He squeaked by with a D average his first year and by graduation had a grade-point average "just north of average." He says he made it on grit, telling himself: "This is a time in life you have to work as hard as before, and you're certainly much better treated." Next came Princeton, then Stanford business school and then, in 1963, Y&R.

Georgescu's 1994 promotion to CE

pped a climb through the ad business lowed by stints as marketing director, en president, of Y&R Inc. Reinvigorating the ad agency, which accounts for % of revenues, has been the highlight his reign. Y&R Advertising has wooed ck AT&T, persuaded Colgate-Palmolive consolidate its worldwide business—rth more than \$500 million—with it, d helped rejuvenate Sears Roebuck th its "Softer Side of Sears" campaign. 1995, the agency won \$1.6 lion in new business.

WAR CHEST. Other units of R Inc.—there are nine in —are also prospering. Bur-n-Marsteller widened its ad as the world's largest blic-relations company in 95, and design company ndor Associates beat its oft projections by a third, part by snagging the

TING Y&R BACK ON TRACK

g Georgescu's accom-plishments:

ocusing the ad on creating ads than dispensing corporate

ding the way toward pay-for-perce ad contracts through deals ears and others.

mpioning globalization of . Won almost all of Colgate-Pal-s international ad ss in the largest consolidation

DATA: BUSINESS WEEK, YOUNG & RUBICAM

tract to create Microsoft Corp.'s ckaging. In 1995, worldwide billings Y&R Inc. were \$10 billion and gross ome rose 15%, topping \$1 billion. Y&R's Aug. 12 announcement of a re-pitalization plan that includes selling minority stake to Hellman & Fried-n, a San Francisco buyout specialist, ds its long run as a 100% employeee-d company. Georgescu says the n was driven by three goals: to buy smaller houses; to invest in online dia, database marketing, and other ngs; and to buy back shares from mer employees, consolidating con-l with current management. "We nt to put together a war chest for quisitions," he says. Hellman & iedman's Warren Hellman says: "Had not thought Peter was sensational, would not have done this deal....He a tremendous natural leader."

As CEO, Georgescu quickly refocused Y&R Advertising on making good ads. In recent years, it had become known as a kind of marketing think tank that turned out safe, uninspired campaigns—"the McKinsey of Madison Avenue," says one insider. Georgescu's message to his executive team: It's time to get humble—before others humble us.

In fact, others had already begun. AT&T and Johnson & Johnson had pulled their business, and by early 1994, the

important now than it has ever been in the history of the human species."

He delivers such pronouncements in idiomatic English cloaked in a velvety East European accent. Georgescu's famous drive is masked by a courtly style that gives him more the air of a professor than an adman. His office bookshelves hold not just predictable fare about branding but also biographies of Niels Bohr and John Maynard Keynes. In conversation, he happily digresses into a 15-minute discourse on the U.S. economy.

About his childhood ordeal, however, he is strikingly taciturn. Most of his colleagues first learned of it when his father died in 1993 and *The New York Times* recounted Valeriu's quest for his sons' freedom. Asked whether, as children, he and Constantin felt aban-



FIRST PITCH: Georgescu and his father and brother with Brooklyn Dodgers Jackie Robinson and Pee Wee Reese on opening day at Ebbets Field in 1954, after the boys were freed from Romania

number of employees had fallen to 720 from 1,200. Now, Y&R has not only won back a good chunk of AT&T's business but has also added 7UP and Blockbuster Videos Inc., among others. Not that everything's perfect. Y&R's work has done little to halt 7UP's slide; Eastman Kodak Co. and Holiday Inn Worldwide went elsewhere in 1995; and Y&R, the largest U.S. ad agency in 1993, currently ranks third. But there's no doubt Y&R is on a roll. "Before he took over, it wasn't as sharp, and there was more internal dissension," says client Stephen A. Cone, chief marketing officer at Key, the Cleveland financial-services company.

Such raves notwithstanding, many companies see ads as an easy cost to cut. That's why Georgescu has become a leading voice for pay-for-performance contracts, in which agency fees are based in part on how well ads work. Y&R says it has earned more on the \$40 million-a-year Sears campaign that way than it would have with a 15% commission.

Georgescu's strategy for the agency is guided by his belief that the slowing of the domestic and global economies over 25 years has made ad agencies indispensable. With massive overcapacity in industries worldwide, selling products is harder, and differentiating goods more critical. "Advertising," Georgescu asserts with no trace of irony, "is more

done by their parents, Peter's response is terse: "They felt guilty. We never felt anger."

Because he was so young, he says, he got away with minor rebellions against his captors, such as mouthing off. He thinks his brother suffered more. Constantin later studied linguistics, worked in the Mideast, and taught. He also worked nine years for the National Security Agency, according to his 1992 obituary. All Georgescu will say is: "He worked for the government. Let's leave it at that."

Some colleagues think Georgescu's childhood experience has left its mark. "He has a peace about him that's very serene, and you don't see that a lot in advertising," says Theodore Bell, the agency's creative head. Georgescu agrees that he was left with an equanimity that persists no matter what's going on around him, whether it's account executives afraid of losing a client or Exeter classmates anxious about an exam. "Having been in a work camp, you don't particularly worry about doing homework past nine o'clock at night," he says dryly. The fact is, Georgescu doesn't seem like somebody who spends a lot of time worrying about anything. That's especially so these days, when there's lots less to fret over at Y&R.

By David Leonhardt in New York

HAS THE NET FINALLY REACHED THE WALL?

America Online's crash may portend constant crises unless the Internet is revamped

It was the day America Online Inc. became America Offline. For 19 hours on Aug. 7, the world's biggest online company and its 6 million customers were blacked out while technicians tracked down what they described as two crippling problems: a faulty roadmap of Internet addresses and a bug in the software of a powerful switching computer called a router. In an apology to subscribers, Chairman Stephen M. Case wrote: "I would like to be able to tell you that this sort of thing will never happen again, but frankly, I can't make that commitment."

That's for sure. Preventing blackouts

may actually get tougher as online services such as AOL—and the global network of networks known as the Internet—run ever closer to the limits of their capacity. Outages at overburdened Internet service providers have already become dismayingly common. Says Allan H. Weis, CEO of Advanced Network & Services, which sold its Internet service business to AOL last year: "Maybe for the first time in the history of the Internet, the demand is exceeding the supply that technology can deliver."

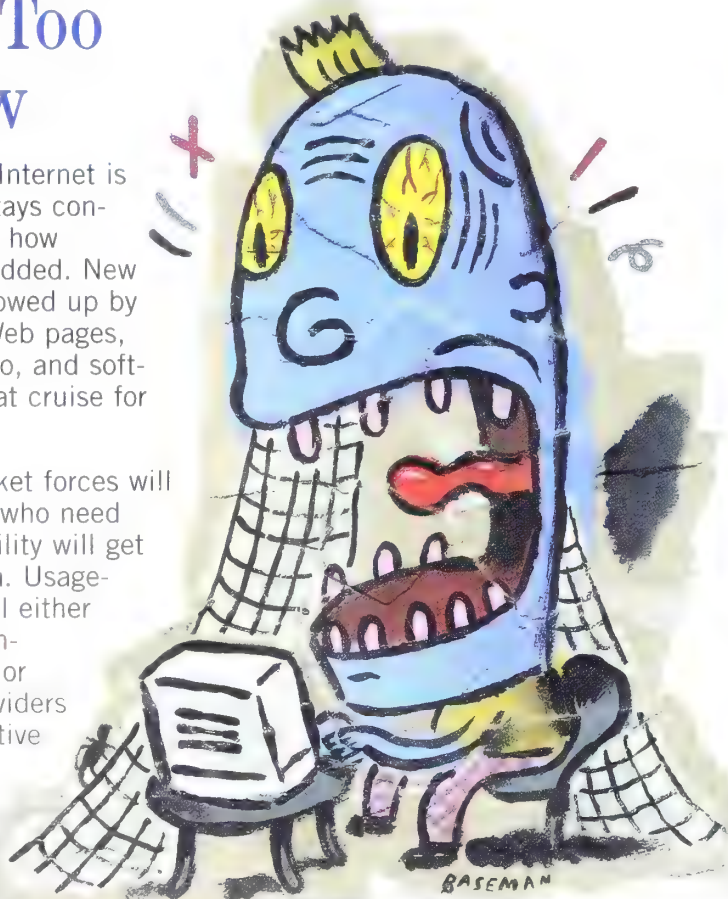
The Net is hardly going to pieces. But the growing pains are so severe that stories about online screwups

could easily carry this headline: "Internet Becomes Victim of Own Success." And service failures are just one problem. Devoted Internauts can reoff a slew of other annoyances: Their favorite Web sites are always busy. Their brand-new modem delivers data like a Volkswagen Beetle on a steep hill. Every newsgroup they visit has been "spammed" with ads for get-rich-quick schemes. They're stymied by fruitless searches for information. They waste hours idly clicking from the Parsons Information Database to the Exploding Head

1 It's Too Slow

PROBLEM The Internet is a highway that stays congested no matter how many lanes are added. New capacity is swallowed up by graphics-heavy Web pages, phone calls, video, and software "robots" that cruise for information.

SOLUTION Market forces will help. Customers who need speed and reliability will get it by paying extra. Usage-based pricing will either kill off bandwidth-hogging services or give network providers a financial incentive to make room for them.



2 Good Stuff

PROBLEM Few Web sites have found a recipe that keeps customers coming back. Search engines that find information are improving but still generate dozens of useless "hits." Sometimes, you're better off going to the library.

ge to acupuncture.com. Aaarrrgh! Yes, the Internet. You can't live with you can't live without it. On one hand, the Net aids scientific collaboration, builds virtual communities, and streamlines commerce—most of the time, without incident. In fact, a BUSINESS WEEK/Harris Poll of 1,186 people taken in 21-30 finds that 79% of those who use the Internet rate the experience excellent or good (page 66). But it's a long way from a mass medium. Today's users are early adopters who tend to be tolerant of glitches. The poll found that while 76% of the U.S. public has heard of the Internet, only half the overall group use a computer at home or work, and only 12% say they have used the Internet or the Web in the past year.

RE TOLLBOOTH. So the Internet still has some growing up to do. Security and reliability must be improved. Technical standards must be established faster, even if less democratically. Lines of control must be clarified. The Internet community must develop ways to settle debates over sensitive issues such as contract law, privacy, and pornography—or risk having governments step into the breach. Intellectual property

must be protected—forget that dippy slogan bandied about the Net that “information wants to be free.”

Above all, financial incentives for investment must come into line. Right now, customers who pay a mere \$20 a month can blast the Net with untold megabytes of data, voice, and video. Without usage-based charges, service providers are called on to upgrade their infrastructure with no clear promise of a return on their investment. For that reason, today's Internet is destined to collapse under its own weight, predicts Edmond J. Thomas, executive vice-president of Nynex Science & Technology Inc., in Price Waterhouse's book, *EMC Technology Forecast: 1997*. It will reemerge, says Thomas, “but there will be a lot more tollbooths on that highway than there are now.”

The Internet's chaotic present stems from its anarchic past. It was never designed to be an all-purpose, for-profit communications network. Its predecessor, Arpanet, was started in 1969 by the Defense Dept. to connect incompatible computers at universities doing military research. The Internet emerged in the 1970s to connect Arpanet with

other networks. There was no need or way to bill for usage, since the government paid for pretty much everything. Besides, the Internet was designed strictly for data, which it breaks into packets that travel disjointedly, to be reassembled at their destination. That's a liability now that the Internet is handling live traffic such as phone calls and videoconferences, where unpredictable delivery times are intolerable.

That's no rap against the pioneers who designed the Internet more than 20 years ago. Phones and electricity fail sometimes, too. The Net has held up remarkably well considering its rapid growth: The number of computers connected to it worldwide is rising 72% a year, according to a recent survey by Network Wizards in Menlo Park, Calif. Operators have to switch out equipment on a monthly or even weekly basis. Such changes can have poorly understood ripple effects, says Columbia University computer science professor Yechiam Yemini. “You don't change one of the engines under the wings of a jet with one 10 times faster and expect the plane to fly. It will crash,” says Yemini.

While there aren't widespread black-

③ It's Not Built Right

PROBLEM The Internet is struggling with missions it simply wasn't designed for. Security is weak. Important traffic gets stuck behind low-priority drivel. It's not well-suited for voice and video. There's no mechanism for counting usage—or charging for it.

SOLUTION New software will let networks give certain traffic higher priority and charge for the service. Encryption will protect credit-card numbers, and digital signatures will unmask people who pretend to be who they aren't.

Hard To Find

PROBLEM Artificial intelligence will make search engines more discerning. People are flocking around to create Web sites will gradually change of the new media. Internet will offer rich the chosen few.



outs, there are frequent brownouts. The Web is already derided as "slow television," or the "World Wide Wait." Imagine the traffic jams when couch potatoes can click through the Web with remote controls—and thousands decide to check out the *Friends* site during a commercial break from the TV show.

Computer experts have worried about Internet overload since its earliest days. But the concerns were easy to dismiss as long as the state of the art was well ahead of the demand. It isn't anymore. Advanced Network & Services' Weis points out that the speed of the Internet backbone rose 700-fold between 1987 and 1992. Another 700-fold increase in the next five years is hard to imagine. "The big problems of the Internet haven't hit yet," says Weis. "We don't know what they are."

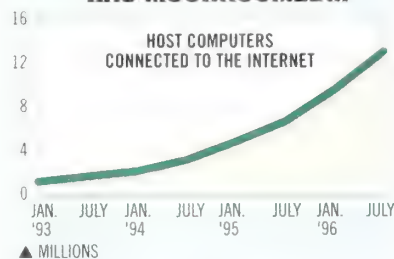
Locating what you want on the Internet is already a challenge, and threats to get harder. The Internet is like a library with no filing system, one that's constantly receiving more books in random piles. Search engines like Yahoo! and Lycos create indexes of the Net's contents by sending software "robots" on search missions—rummaging through the growing piles again and again. That works O.K. on small databases, but 'bots can be mighty annoying on big ones. When they hit Los Alamos National Laboratory, some poorly programmed robots get lost inside a vast database of physics research, tying up the lab's computers by issuing up to 10 information requests a second.

DIRTY SECRET. The Internet is beginning to suffer from a lack of manners as well. One dirty little secret is that most phone calls and videoconferences ram their way past data transmissions by using a bully of a communications method called User Datagram Protocol, or UDP. Unlike the more polite Transmission Control Protocol, TCP, which drops back when it detects congestion, UDP continues at full speed, elbowing ahead of TCP traffic. Yet UDP customers aren't paying anything extra for their fast lane. What's to stop it from being abused? "It's really basically altruism and peer pressure and people knowing each other," says Jeffrey K. MacKie-Mason, an associate professor of economics, information, and public policy at the University of Michigan.

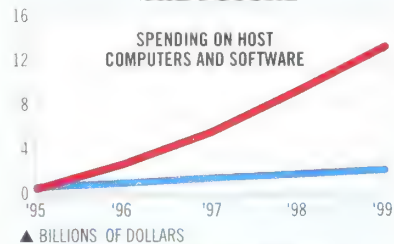
Altruism is hardly a workable ethic for an Internet that has be-

come huge, impersonal, and profit-minded. The Net's deficiencies are reflected in the lives of people like Rick Cunningham, a mechanical engineer from Chandler, Ariz. After discovering the Internet, he says, "I jumped into it with both feet," using it to plan a vacation, exchange E-mail, and weigh investments. But when he researched the purchase of a water softener, all he got was product puffery. And he spent five hours over three days searching for historical stock data. Finally, he got off the Information Superhighway, into his car, and onto Interstate 10, down to the Phoenix public library. There, he spent less than an hour getting the information from microfilm. Cunningham's advice about cruising the Net: "Take your sleeping bag."

WHILE THE INTERNET HAS MUSHROOMED...



...INTRANETS ARE THE FUTURE



DATA NETWORK WIZARD; ZONA RESEARCH INC.



It's a bad sign when the likes of Cunningham get disillusioned. A survey by Mercer Management Consulting Inc. identified only two groups making up 17% of the population—the "Wired Elite" and "Upgrade Families"—that account for two-thirds of the market for electronic commerce and network-based services. Says Mercer Vice-President Michael E. Smith: "You're probably talking about a cap of 25% to 30% of the households that are really willing to step up to the plate to put up with the difficulties." Forrester Research Inc. in Cambridge, Mass., predicts that the average Web publisher will lose money until the year 2000. "Content providers who join the Web gold rush find themselves tumbling down a long, dark mine shaft," writes Senior Analyst Bill Bass.

CLEARER PATH. Internet skeptics—perhaps realists—are redirecting the money away from the Net and toward private "intranets," where they see a clearer path to profitability. These internal networks work like the Internet and can communicate with it but are built for a company's own employees, big customers, and suppliers. Intranets aid collaboration by pulling together data of incompatible computers. Zona Research Inc. in Redwood City, Calif., predicts that in 1999, spending on host computers and software for intranets will exceed Internet spending by 6 to 1 (chart).

The Internet, in contrast, suffers from topsy-turvy financial incentives because of its legacy as a government-subsidized enterprise. Big Internet service providers such as MCI Communication Corp. and Sprint Corp. have long accepted traffic from many of the smaller ones without demanding payment. But that practice has become onerous. So they're raising standards for admission to the club of "peers" that exchange traffic for free. All others must pay.

That change will spill over to the way carriers charge their customers. If one carrier is charged by others for sending them lots of, say, video signals, it will turn around and raise the fees for that kind of traffic. Such usage-based payment will discourage capacity-hogging traffic that doesn't make economic sense. And it will raise money for investment to support other services that do make sense—phone calling, perhaps.

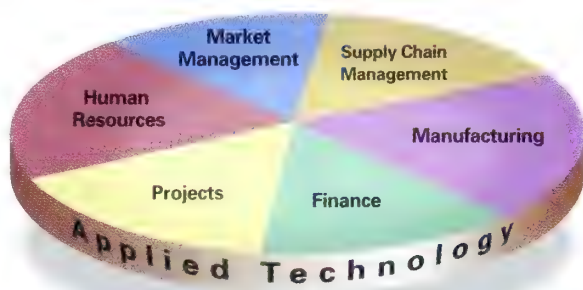
The next step is to get the phone companies and cable-TV operators to

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invest more. Today, says Roger S. Siboni, national managing partner of KPMG Peat Marwick, the carriers that provide Internet infrastructure "are fearful that they'll be segmented out of the value proposition—they'll be reduced to a commodity while others will add value."

If phone companies don't hold back the Internet, standards wars might. Net standards have long been set by a collegial group of volunteer experts known as the Internet Engineering Task Force. But more companies with a stake in the Net's development are sending delegates to IETF committee meetings. That bogs things down because anyone who attends has a vote, no questions asked.

Meanwhile, standard-setting for the World Wide Web is beset by fighting

between Microsoft, Sun Microsystems, and Netscape Communications. Tim Berners-Lee, the research scientist who is credited with inventing the Web and now directs the World Wide Web Consortium, says he worries that in their efforts to one-up each other with unique features, these rival companies could spoil things for their customers.

The battling creates headaches for people who need to place bets on which technologies will take hold. Trouble is, no one really runs the Internet. "The framework that people cooperated in before is collapsing, and a new framework has to emerge," says Robert G. Moskowitz, a technical support specialist for Chrysler Corp., a big Internet user. So the Internet is at a turning point.

It has certainly impinged upon the public's consciousness—AOL's Aug. 7 crash made front-page news across the country. Moskowitz recalls that in the early 1950s, the American public turned against the space program after a Redstone rocket blew up on the launchpad on live television. "There is a concern in the Internet technical community that we can lose the consumer. This is completely recognized." His prediction: "We'll get things straightened out." The community has a powerful incentive to do just that. After all, worrisome as they may be, the Internet's problems stem not from decline, but growth.

By Peter Coy in New York, with Robert D. Hof in San Francisco, Patricia C. Judge in Boston, and bureau reporters

BUSINESS WEEK/HARRIS POLL

INTERNET TRAVELERS AREN'T FED UP—YET

People who jump into cyberspace are generally happy with what they get. Just under 20% of adults have used the Net or the World Wide Web in the past year, according to a poll conducted June 21-30. Of those, 79% rated their experience good or excellent. Nearly two-thirds of Internet



users say they expect to use the Net or the Web a lot in the coming year. But the online world has its flaws: More than half say slow access, high cost, and difficulties in connecting and locating information are problems. Of course, these are the views of the early Internauts, who may be more tolerant of glitches; the masses could be less forgiving.

ARE YOU EXPERIENCED?

Do you use a computer at home, at work, or at another location, or not?

Use a computer.....	50%
Do not use a computer	50%

THE CYBER-CONSCIOUS MASSES

Have you ever seen, read of, or heard of the Internet, or not?

Have seen, read of, or heard about the Internet.....	87%
Have not seen, read, or heard	13%

A MINORITY OF WEB CRUISERS

Have you used the Internet or the World Wide Web in the past 12 months, or not?

Used in past 12 months.....	19%
Not used	31%
Don't use computer	50%

[Remaining questions were asked only of those who have used the Internet or the Web in the past 12 months]

PROBLEMS FOR THE FAITHFUL

Now, I'd like to ask you about possible problems you might

have with the Internet or the World Wide Web. Is each of these a major problem, a minor problem, or not a problem at all?

	MAJOR PROBLEM	MINOR PROBLEM	NOT A PROBLEM	DON'T KNOW
Slow access	28%	45%	26%	1%
High cost	24%	32%	43%	1%
Information difficult to locate	19%	47%	34%	0%
Difficult connections	17%	44%	38%	1%
Content isn't interesting	8%	28%	63%	1%

FREQUENT FLIERS

How often are you likely to use the Internet or the World Wide Web in the coming year—a lot, a few times, or not at all?

A lot.....	65%
A few times.....	32%
Not at all	3%

MANY SATISFIED SURFERS

How would you rate your experience with the Internet or the World Wide Web—excellent, good, fair, or poor?

Excellent	16%
Good	63%
Fair.....	20%
Poor	1%

EDITED BY KEITH H. HAMMONDS

Survey of 1,005 adults, plus an additional 181 adults who have used the Internet or World Wide Web in the past 12 months, conducted June 21-30, 1996, for BUSINESS WEEK by Louis Harris & Associates Inc.

HOW TIFFANY'S TOOK THE TARNISH OFF

Chaney restored the brand's cachet and widened its reach

William R. Chaney, the understated chief executive of Tiffany & Co., has spent 12 years cultivating the Tiffany brand with a slow but steady hand. In a business full of glitz and glamor, he prefers to let results do the dazzling. "We've had a very consistent direction and strategic plan," says Chaney. "It's business 101."

That's a course that seems to be working. Over the years, Chaney, 64, has increased the New York-based retailer's presence, polished Tiffany's image, and launched aggressive marketing campaigns to widen the appeal of Tiffany's blue box beyond blue-blooded shoppers. With much of the retail sector still in the doldrums, the benefits of Chaney's steady efforts are shining bright. Despite a shaky retail environment, Tiffany's sales in U.S. stores open a year or more grew 12% last year and jumped another 20% for 1996's first quarter.

Although the early 1990s recession had a costly buyout of its Japanese partner caused a \$10 million loss in 1993, Tiffany has been sparkling ever since. Fueled by a rebound in the luxury-goods market, sales hit \$803 million for the 95 fiscal year ended in January, 1996, a 6% gain over the year ended in January, 1993. Tiffany's operating income tripled, to a record \$80 million, for the same period, and Oppenheimer & Co. analyst Dorothy Lakner thinks it will reach \$102 million this year.

MAIL-ROOM START. Investors' results are also gleaming. After lagging around 10% for most of the early 1990s, Tiffany's adjusted shares have more than doubled, to around 34%, since mid-1995. Chaney has expanded around the world, merchandised correctly, managed the financials, and he's a nice guy to boot," says Douglas C. Eby, portfolio manager at Robert E. Torrey & Co., which owns 1.3 million shares.



GOLDEN AGE?

CEO Chaney says there's room for 20 more domestic stores. But much of the growth will come overseas

Now the trick will be keeping up the sterling performance even if the U.S. economy slows. But that's a challenge Chaney, who led a leveraged buyout of Tiffany from Avon Products Inc. in 1984, relishes. He began his 28-year Avon career as a supervisor of the Kansas City mail room. Chaney soon jumped to sales, and by 1984 he'd landed the chairman's job at Tiffany. It was then an unprofitable eight-store chain with a small Japanese wholesale business and a tarnished image. Avon had acquired the publicly traded company in 1979 and neglected the now 159-year-old brand by

skimping on customer service. Seeing a diamond in the rough, Chaney got backing from Investcorp, a Bahrain-based investment bank, for the LBO. It took Tiffany public again in 1987.

Chaney's first move was to restore Tiffany's luster. Increased staffing improved customer service, and he then began more frequent inspections of merchandise for quality. Recognizing Tiffany's overdependence on the New York store—which contributed roughly 40% of total revenues in 1988—Chaney launched a worldwide expansion. In 1993, he took control of the Japanese operation, now Tiffany's most profitable area (page 68). Today, Chaney presides over a network of more than 100 Tiffany shops in 16 countries and wholesales its products in 30 others. The U.S. contributes 62% of sales and 47% of profits before corporate expenses.

TRICKY. Chaney's trickiest challenge has been maintaining Tiffany's elite image while trying to draw a wider array of customers. To do so, Chaney has launched ambitious marketing campaigns, with such offerings as "How to Buy a Diamond" and "Pearl Authority." His goal: convince buyers of Tiffany's quality and make it seem attainable. "We have a democratic vision," says President Michael J. Kowalski, who is Chaney's heir apparent and the man behind the marketing push. "We want people to aspire to be a customer, but never to feel excluded."

Keeping snobbery in check has proven lucrative. The average retail transaction in fiscal 1995 was a relatively reasonable \$256. Indeed, less than 5% of Tiffany's sales come from items costing \$50,000 or more. Even competitors are fans. "Tiffany is first-class," says Francesco Trapani, CEO of Bulgari Group. "They maintain the balance between availability and scarcity."

Typical of the newest customer is Joseph Day, a New York optician who bought a \$54 silver Tiffany "bean" necklace for his girlfriend. "There are things for a million dollars and things for \$20," he says. He's right: Products range from a \$15 box of playing cards to a \$1.85 million triple strand of South Sea pearls. Tiffany now rolls out at least three new lines a year. One recent hit was the Atlas Collection, a watch and jewelry line with prices ranging from \$95 to \$15,000.

With such moves bringing a steady stream of new customers, Chaney says there's demand for at least 20 more do-

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SHOWCASE

Japan's recession didn't dent Tiffany. Today, Japan contributes 28% of the retailer's revenues and 53% of operating profits before expenses

New York-based jeweler realized it was going out. Although Tiffany had a wholesale business, Mitsukoshi had juicy margins at retail. And demand grew even as Japan's economy slowed, a struggling Mitsukoshi couldn't invest in expansion. So Tiffany paid \$115 million for its Japanese operations and inventory. The mostly buyout handed Tiffany a small loss in 1993, but the shift paid off. While Tiffany has kept its stores at Mitsukoshi and at rival department store Daimaru Inc., it now earns an operating fee based on sales and keeps the rest. And Tiffany's 7,000 square feet in Ginza, the priciest district, for its compact store—three times the size of

a Mitsukoshi boutique. That lets Tiffany display more and offer something for every wallet.

The result: Yen-denominated sales in stores open a year or more grew 13% in 1995—and Japan is now the brightest jewel in Tiffany's tiara. With sales of \$226 million, Japan made up 28% of Tiffany's revenues last year, up from 19% in fiscal 1993. Better yet, higher prices helped Japan bring in 53% of Tiffany's operating profits (before corporate expenditures) last year. At \$68 million, that's more than double its 1993 profits. "Other businesses have suffered [from the recession]," says Thomas J. O'Neill, senior vice-president of international sales, "but we haven't."

That's partly because of people like

Yumiko Murayama and fiancé Shinjiro Yokoyama, one of several couples crowding a wedding-band display. "It isn't so very expensive," Yumiko giggles, glancing coyly at her betrothed. Wedding-related items bring in more than 35% of sales, and it's not just rings. At Japanese weddings, guests bring money, and the newlyweds give them gifts, called *hikidemono*. One hot item is a \$72 Imperial cup and saucer set. With families buying in bulk, *hikidemono* means big sales at retail prices. "We're going after the bridal market in a big way," O'Neill says.

Ginza is just the start of Tiffany's push into Asia. O'Neill says he's looking for an Osaka site. And since June, it has opened stores in Singapore, Hong Kong, and Korea, with plans for up to 10 more by 2001. Yet if Tiffany becomes too accessible, it may dilute its appeal among shoppers who like traveling long distances for their status symbols. "The designs are better overseas—and cheaper too," sniffs Nakano. But if young waitresses can be so discriminating, Tiffany will do just fine.

By Edith Hill Updike in Tokyo

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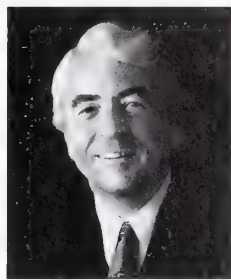
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EDITED BY AMY DUNKIN

LEAVING YOUR JOB? WEIGH YOUR 401(k) OPTIONS

When Senior Editor Becky Cabaza left Bantam Books for Simon & Schuster in 1993, she didn't rush to transfer her 401(k) money into her new employer's plan. Thanks to previous job-hopping, she knew she should investigate her options before making a move. And it was a good thing she did.

She discovered that not only did Simon & Schuster offer fewer investment choices than Bantam, but getting answers to her questions about the mutual funds in the plan proved near impossible. As a result, she decided to leave her account with Bantam. More recently, Simon & Schuster overhauled its retirement savings program. With greatly improved investment options and service, Cabaza is now contemplating rolling the Bantam money over.

If Cabaza learned one thing from moving around, it's that she shouldn't let her 401(k) get lost in the shuffle. Yet too often, the last thing job-hoppers think about are their 401(k) plans. Considering that these accounts represent the bulk of most people's retirement savings, managing these assets should be a top priority—not an afterthought.

TEMPTATION. When leaving a company, you have several ways to handle your 401(k): cash out, leave the account where it is, join your new employer's plan, or roll over the assets into a bank or brokerage IRA. Most people take the money and run—but that's by far the worst option. A 1995 Labor Dept. study found that 68% of peo-

ple over age 40 and 84% of those under 40 fail to roll their retirement funds into another tax-deferred vehicle when they change jobs. The temptation to get your hands on a big wad of cash is understandable, but the taxes and penalties on early withdrawals should be enough to kill any desire. If you take a lump-sum distribution and are under age

59½, the Internal Revenue Service will withhold 20% in anticipation of the income tax you'll have to pay—plus a 10% penalty on the proceeds.

Well before leaving your old job, you should find out whether your new employer has a 401(k) and will accept rollovers. If so, don't just dive into the new plan. Assess all your options, comparing the investment quality and flexibility of each. A well-designed plan offers a broad range of investments—from a conservative money-market fund to a menu of equity and bond funds—and the ability to transfer among them at no cost, says Julie Jason, author of *You & Your 401(k)* (\$10, Fireside Books, 800 223-2336). It's important to read the plan summary, especially the sections on distributions and hardship withdrawals. Detailed, timely account statements and loan features are also key elements of a good plan.

Like Cabaza, you might find that your old plan offers a hard-to-beat combination of investment diversity, superior customer service, and other attributes. If your balance is more than \$3,500, you're entitled to keep your account with your former employer until age 70½, when you must

begin taking mandatory minimum distributions. When making your decision, take into account any restrictions the old plan imposes on money left behind. "The rules will vary enormously," says Rich Koski, a principal at Buck Consultants in Secaucus, N.J. "Some companies will charge you an administrative fee or restrict your access to the account and any new investment options." Also keep in mind that you will no longer be able to make contributions to that particular account.

PENALTIES. One situation in which you might want to stay with the old 401(k) is if you have an outstanding loan against it and your former employer will let you continue repayment after you leave.

However, most companies require that the loan be repaid in full immediately upon termination, so it's a good idea to investigate other repayment options well in advance. If you are unable to pay on the loan, the outstanding balance will be deducted from your account and subject to tax and penalty. For example, if your 401(k) total is \$100,000 and you have an outstanding loan of \$40,000, your employer will take \$40,000 from the account and use it to satisfy the loan. The IRS then treats that money as a distribution on which you owe income tax—plus that 10% penalty if you're under age 59½. The remaining \$60,000 should be handled like any other 401(k) and left in the original account or rolled over into a new plan or IRA within 60 days.

A way around all this, your new plan has a loan feature, is to arrange a short-term personal or home-equity loan before you change jobs, says David Wray, president of the Profit Sharing/401(k)



Finding the Best Fit

There are the three choices for handling your 401(k) money when you leave a job. Of course, you can liquidate the account, but the taxes and penalty are so prohibitive that it is strongly discouraged.

STAY WITH ORIGINAL 401(K)

If you have an account balance of more than \$3,500 and your new plan doesn't accept rollovers

If the new plan has limited investment and distribution options, poor investor services, and no loan or hardship withdrawal provisions

If you've taken a loan against the plan and you can't continue paying it off

ROLL OVER INTO NEW EMPLOYER'S 401(K)

If it has superior investment options and flexibility to move money among funds

If it offers a loan feature and hardship withdrawal policy

If the plan administrator provides good investor service and timely account statements

TRANSFER MONEY TO AN IRA

If you have an account balance over \$10,000 (usually the minimum needed to qualify for no-fee IRAs at discount brokerages) and want a broader selection of investments

If the new plan doesn't allow rollovers

If both the new and old plans offer limited investment selection, access to loans, or account status reports

DATA: JULIE JASON, AUTHOR OF *YOU & YOUR 401(K)*



Council of America in Chicago. You can use that money to pay off the 401(k) loan and roll over the full 401(k) balance into your new plan. Then, you can take out a loan against your new plan to pay off the outside financing.

But if both the old and new 401(k) plans are unsatisfactory, or you simply want more control over your investment choices, consider opening an IRA, says Manuel Bernardo, director of employee benefits at Deloitte & Touche in Stamford, Conn. An IRA is the only other way to maintain the tax-deferred benefits of a 401(k) and avoid taxes and penalty.

The major advantage of an IRA is flexibility. "With the advent of no-transaction-fee mutual funds and no-fee IRA programs, you can get access to thousands of funds and 24-hour service," says Will Bashan, president of Cigna Financial Partners in Hartford.

Each time Curtis Shaw, 47, got a new job, he rolled over his 401(k) money into an IRA. "I'd rather be able to direct the investment myself than be limited to the options any new plan provided," says

Shaw, counsel for Nynex Corp. in White Plains, N.Y. He has invested his IRA in everything from zero-coupon bonds to individual stocks.

While rollover IRAs offer more investment selections than a 401(k), you lose the ability to make additional contributions (except for rollovers from other qualified plans), borrow against your account, or protect your assets. "If you have existing debts or potential exposure to lawsuits, a 401(k) offers greater protection from creditors' claims than an IRA," says Kenneth Brier, a tax attorney

with Sherburne, Powers & Needham in Boston.

When considering an IRA rollover, beware of consultants bearing bad advice. Employers frequently offer departing workers financial-education seminars, which all too often become forums for investment sales pitches. At one such gathering, a financial adviser solicited a 56-year-old man with a \$560,000 401(k) and convinced him to put all the money in a "no-load" variable annuity. While it sounded good in theory, the man didn't realize he would be paying an additional 1% per year in fees for an extra layer of tax deferral that he didn't need.

COSTLY MISTAKE. If you choose an IRA, the first step is to set up a segregated account for tax purposes, says Wendy Blank, a financial planner with Blank Financial Group in New York. As long as you do not mix your rollover account with other qualified-plan assets, you'll still be able to bring that money into your new company's 401(k) plan later. Then, you'll need to instruct the 401(k) administrator to transfer assets directly to your new IRA instead of cutting you a check. If you receive a check, the company must withhold 20% of the money. To continue tax-deferral benefits, you will need to deposit the check with your IRA custodian within 60 days, says Jason, the author. And you'll need to add the 20% that was withheld into the IRA or that 20% will be considered a distribution subject to taxes and the 10% early-withdrawal penalty. As long as you make the account whole, the IRS will refund the withheld 20%.

Now that 401(k) plans have been around for nearly two decades, participants who contribute regularly are astonished by how much they have managed to save. So if you change jobs and don't carefully consider how to handle your 401(k) money, you could be setting yourself up for a costly mistake. *Kerry Capell*

BARGAINS ON THE WORLD'S BOURSES

The big scare that rocked Wall Street in July has given way to the languor of August. Even traders who aren't on vacation are more relaxed, as recent economic data have temporarily calmed fears of a hike in short-term interest rates before November's Presidential election.

But the operative word is "temporarily." The U.S. market isn't out of the woods, and a couple of scary numbers on spending or wage growth could cause another round of jitters. That's why many fund managers are looking at foreign stocks as an alternative. They argue that while the next move from the Federal Reserve is more likely to be up than down, interest rates abroad will probably stay low to stimulate economies that in many cases are struggling to break out of recession. That bodes well for growth and corporate profits abroad. Over the next year, says William Sterling, chief strategist for New York money manager BEA Associates, "we'll see foreign markets making good gains while the U.S. does nothing."

ON THE PROWL. Some money managers view the current lull as an opportunity to bargain-hunt. Just ask Bruce Bee, a money manager in Denver who specializes in small-capitalization stocks. He's snapping up shares of such overlooked companies as Stratec Holding, a Swiss maker of orthopedic equipment that boasts a stellar 30% return on equity but is trading in

Geneva at a price-earnings ratio of only 4.

Bee is also on the prowl for underperforming European companies that are expected to slim down. In the financial sector, strategic shifts at Deutsche Bank, CS Holding, and Swiss Bank, among others, are sparking speculation that even more

SMART MONEY

industry restructuring is on the way. One possible winner, notes Montgomery Asset Management Managing Director John Boich, is Paris-listed Crédit Commercial de France. Despite 15% annual

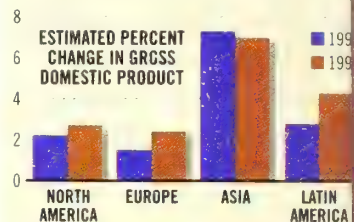
earnings growth, CCF sells at book value—half the valuation of some larger European competitors—in part because of the taint of France's troubled banking sector. Boich feels CCF could become a takeover target for another French bank eager to get its hands on its successful fund-management business.

PHONE FAN. Others think richer treasure lies buried in the developing world. "There still are screaming buys on emerging markets, particularly in Latin America," says Richard Johnston, a managing director at New York-based Offitbank. Johnston is particularly enthusiastic about prospects for the Brazilian and Peruvian phone companies, Telebras and Telefónica de Peru. Both companies, he says, boast annual earnings growth of about

Jakarta exchange, and Thailand's Ayudhya Insurance Public Co., a property/casualty insurer listed in Bangkok.

The perception that the Federal Reserve will lead interest rates alone for now makes such emerging markets even more attractive.

GROWTH WILL BOOST FOREIGN EXCHANGES



DATA: DEUTSCHE BANK RESEARCH ESTIMATES

since their fortunes are heavily dependent on U.S. monetary policy. That's why Charles Asset Management's chief investment officer, Mark Richardson, recently increased his holdings in Latin America and East Asia. In Europe, Richardson believes there could be another round of interest rate cuts this fall as central banks try desperately to get growth rates back up above 1%, and he thinks European markets offer "fundamentally decent value." He is also moving money into consumer, leisure media, and property stocks in Japan, whose economy may expand by around 2.5% this year and next after four years of slump.

You don't have to be a fund manager to invest in offshore stocks. Even if a company hasn't issued ADRs, most major brokers will buy and sell shares on foreign bourses. A thoughtful broker will remind you, of course, that as the weakening of the dollar against the other country's currency could diminish or wipe out your stock gain. But if the economic-growth argument holds up, venturing abroad will be well worth that risk.

William Glasgall and Joe Warner



25% and, as a bonus, trade in the U.S. through American depositary receipts. Yet each is trading at a p-e of 9—nearly half the current ratio for the Dow Jones industrial average.

Gary Greenberg, deputy managing director of Peregrine Asset Management (Hong Kong) Ltd., is combing through Asian markets for fast-growth stocks. He's finding them in insurance, an industry just taking off in many developing countries. Greenberg is recommending Indonesia's Lippo Life Insurance, a local provider that trades on the



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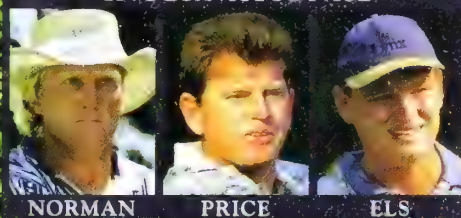
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TELEVISION TIMES

September 12	Thursday	5:30 p.m. - 6:00 p.m.
September 13	Friday	8:00 a.m. - 12 noon, 2:00 - 6:30 p.m.
September 14	Saturday	2:00 p.m. - 6:00 p.m.
September 15	Sunday	1:00 p.m. - 6:00 p.m.

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TICKET INFORMATION

Attendance will again be limited to the first 18,000 ticket holders.

Tickets may be purchased at all George Mason Banks, Washington Golf Centers, PGA TOUR Shops at Tyson's Corner and Union Station, Paradies Shops at Dulles and Washington National Airports or by calling 703-754-1110 or

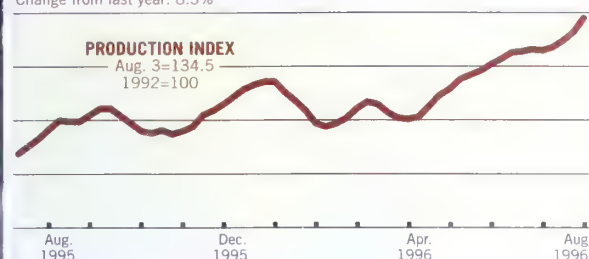
1-800-668-6875



Business Week Index

PRODUCTION INDEX

Change from last week: 1.0%
Change from last year: 8.3%



The index is a 4-week moving average.

The production index increased during the week ended Aug. 3. Before calculation of the four-week moving average, the index also increased, to 131.6, from 131.1. For the month of July, the index advanced to 133.9, from 131.6 from June. Data collection of paper and paperboard output has been discontinued and will no longer be included in the production index.

The leading index will be unavailable for an indefinite period of time.

Production index copyright 1996 by The McGraw-Hill Companies.

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
CLOCK PRICES (8/9) S&P 500	662.10	662.49	18.5
CORPORATE BOND YIELD, Aaa (8/9)	7.53%	7.73%	-2.3
INDUSTRIAL MATERIALS PRICES (8/9)	107.5	107.3	-5.7
BUSINESS FAILURES (8/2)	NA	NA	NA
REAL ESTATE LOANS (7/31) billions	\$522.8	\$522.5	6.3
MONEY SUPPLY, M2 (7/29) billions	NA	NA	NA
INITIAL CLAIMS, UNEMPLOYMENT (8/3) thous.	318	294r	-2.2

Sources: Standard & Poor's, Moody's, *Journal of Commerce* (index: 1990=100), Dun & Bradstreet (failures of large companies), Federal Reserve, Labor Dept.

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (8/13)	4.89%	5.10%	5.74%
COMMERCIAL PAPER (8/13) 3-month	5.40	5.43	5.85
CERTIFICATES OF DEPOSIT (8/14) 3-month	5.39	5.40	5.80
FIXED MORTGAGE (8/9) 30-year	8.15	8.41	8.02
ADJUSTABLE MORTGAGE (8/9) one-year	5.98	6.14	5.91
TIME (8/13)	8.25	8.25	8.75

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

INTERNATIONAL TRADE

Friday, Aug. 20, 8:30 a.m. EDT ▶ The trade deficit for goods and services narrowed in June to \$9.3 billion, an unexpectedly large \$10.9 billion in May. That's the median forecast of economists surveyed by MMS International, one of McGraw-Hill Companies. Exports, which increased 1.1% in May, are expected to have risen further, while imports probably fell back after climbing strongly for five months in a row.

FED MEETING

Friday, Aug. 20 ▶ By a wide margin, the economists expect no action at the policy meeting of the Federal Reserve's

Open Market Committee. That means the Fed will keep its target for the federal funds rate—the cost of overnight borrowing by member banks—at 5.25%. The central bank last moved short-term interest rates on Jan. 31, when it cut the fed funds rate by a quarter-point. The consensus view among economists now is that any future move will be to raise rates.

FEDERAL BUDGET

Wednesday, Aug. 21, 2 p.m. EDT ▶ The Treasury Dept. will probably announce a budget deficit of \$25 billion in July. In July, 1995, the deficit totaled just \$13.6 billion, but that's because the first of the month fell on Saturday and Social Security checks were

sent out in late June, 1995. The deficit is on track to end fiscal 1996 below \$120 billion, from \$164 billion in 1995. But on Aug. 12, the Congressional Budget Office released a report warning that federal red ink would begin to flow faster again in 1997 and reach \$285 billion by 2002 if no changes are made to fiscal policy.

DURABLE GOODS ORDERS

Friday, Aug. 23, 8:30 a.m. EDT ▶ New orders taken by durable-goods manufacturers likely rebounded by 1% in July, after dropping 0.6% in June. Rising demand for motor vehicles likely led the gain. Unfilled orders, which rose 0.6% in May and June, probably increased again in July.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (8/10) thous. of net tons	1,936	2,022#	0.9
AUTOS (8/10) units	124,057	124,381r#	19.8
TRUCKS (8/10) units	108,956	105,366r#	1.2
ELECTRIC POWER (8/10) millions of kilowatt-hrs.	75,365	71,810#	1.2
CRUDE-OIL REFINING (8/10) thous. of bbl./day	14,423	14,299#	1.3
COAL (8/3) thous. of net tons	19,032#	19,525	5.2
LUMBER (8/3) millions of ft.	482.3#	486.9	10.8
RAIL FREIGHT (8/3) billions of ton-miles	25.9#	26.4	4.0

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWPAl, SFFPAz, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (8/14) \$/troy oz.	386.700	388.000	0.9
STEEL SCRAP (8/13) #1 heavy, \$/ton	139.50	134.00	-4.8
COPPER (8/10) ¢/lb.	96.2	96.2	-31.3
ALUMINUM (8/10) ¢/lb.	71.4	71.0	-19.3
COTTON (8/10) strict low middling 1-1/16 in., ¢/lb.	74.72	76.95	-8.5
OIL (8/13) \$/bbl.	22.45	21.19r	28.9
CRB FOODSTUFFS INDEX (8/13) 1967=100	343.52	340.56	1.5
CRB RAW INDUSTRIALS INDEX (8/13) 1967=100	282.00	275.17	20.9

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (8/14)	107.81	107.79	97.55
GERMAN MARK (8/14)	1.48	1.48	1.47
BRITISH POUND (8/14)	1.55	1.54	1.54
FRENCH FRANC (8/14)	5.07	5.06	5.06
ITALIAN LIRA (8/14)	1516.5	1519.5	1619.5
CANADIAN DOLLAR (8/14)	1.37	1.37	1.36
MEXICAN PESO (8/14) ³	7.468	7.494	6.225

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars

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BusinessWeek

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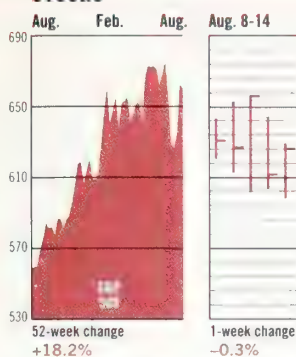
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Investment Figures of the Week

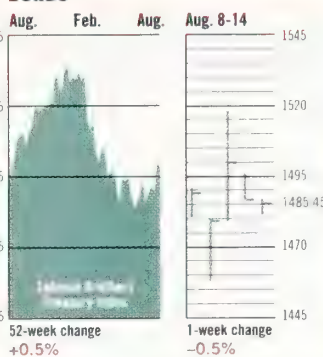
STOCKS

Stocks plunged after Philip Morris Cos. found negligent in a case involving a smoker who developed cancer. Philip Morris Cos. saw its stock fall 14%, to 91%, which cut the company's market capitalization from \$87.7 billion to \$77 billion. The broader markets were spooked by jumps in consumer prices and retail sales fanned inflation fears. Still, yields on the 30-year Treasuries moved for the week—up two basis points.

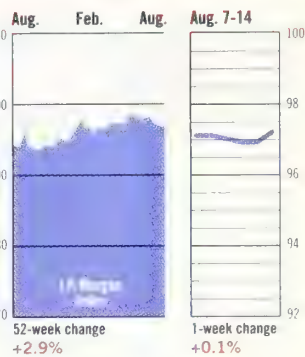
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
JONES INDUSTRIALS	5666.9	-0.9	22.2
DOW JONES (S&P MidCap Index)	229.6	0.4	9.7
DOW JONES (Russell 2000)	326.7	-0.3	8.1
DOW JONES (Russell 3000)	375.2	-0.3	16.4

FOREIGN STOCKS	Latest	% change (local currency) Week	% change 52-week
DOW JONES (FINANCIAL TIMES 100)	3832.0	0.5	10.6
DOW JONES (NIKKEI INDEX)	20,981.1	2.5	15.5
DOW JONES (TSE COMPOSITE)	5048.8	0.3	9.6

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.17%	5.16%	5.57%
30-YEAR TREASURY BOND YIELD	6.79%	6.77%	6.88%
S&P 500 DIVIDEND YIELD	2.18%	2.17%	2.39%
S&P 500 PRICE/EARNINGS RATIO	18.9	19.0	16.2

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day moving average	638.8	636.8	Positive
Stocks above 200-day moving average	53.0%	55.0%	Neutral
Speculative sentiment: Put/call ratio	0.57	0.57	Negative
Insider sentiment: Vickers sell/buy ratio	1.66	1.97	Positive

BLOOMBERG FINANCIAL MARKETS

INDUSTRY GROUPS

MONTH LEADERS

	% change 1-month	% change 12-month
40s	14.4	23.5
COMPUTER SYSTEMS	14.3	3.8
METAL AND GLASS CONTAINERS	12.5	3.1
COMPUTER SOFTWARE	10.8	30.8
YS	9.9	13.7

Strongest stock in group

	% change 1-month	% change 12-month	Price
HUMANA	17.8	2.0	19
COMPAQ COMPUTER	30.1	7.9	56 1/4
CROWN CORK & SEAL	15.0	11.0	48
COMPUTER ASSOCIATES INTL.	28.2	67.9	55 1/8
MATTEL	11.3	13.5	27 1/8

MONTH LAGGARDS

	% change 1-month	% change 12-month
BACCO	-10.8	22.0
OIL AND GAS DRILLING	-9.0	67.3
OIL WELL EQUIPMENT AND SERVICES	-7.1	28.5
DEFENSE ELECTRONICS	-6.2	51.6
INTERNATIONAL OIL	-5.6	19.1

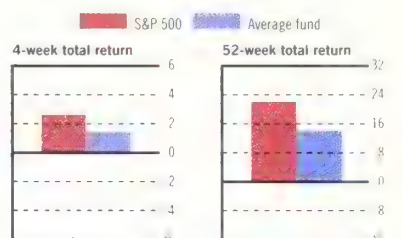
Weakest stock in group

	% change 1-month	% change 12-month	Price
PHILIP MORRIS	-11.7	25.0	90
ROWAN	-17.3	101.8	14 3/4
BAKER HUGHES	-14.1	40.0	29 3/4
EG&G	-6.2	0.0	19
EXXON	-9.7	17.1	81 1/4

MUTUAL FUNDS

LEADERS	Week total return	%	LAGGARDS	Four-week total return	%
NORTHERN TECHNOLOGY	10.0		PIONEER INDIA B	-11.2	
ROWE SCIENCE & TECHNOLOGY	9.9		FIDELITY SELECT NATURAL GAS	-9.3	
BERTSON STEPHENS INFORMATION AGE	9.4		EV TRADITIONAL GREATER INDIA	-7.9	

	Week total return	%		52-week total return	%
NDMARK SMALL CAP EQUITY A	66.2		STEADMAN TECHNOLOGY GROWTH	-35.0	
UNITREND GOLD	57.4		UNITED SERVICES GOLD SHARES	-22.0	
RNER SMALL CAP EQUITY	52.7		RESERVE INFORMED INVESTORS GROWTH A	-19.2	



MORNINGSTAR INC.

RELATIVE PORTFOLIOS

Relative amounts represent the relative value of \$10,000 invested one year ago in each portfolio.

Percentages indicate daily total returns.

U.S. stocks
\$12,056
-0.33%

Foreign stocks
\$11,233
-1.03%

Treasury bonds
\$10,861
-0.68%

Money market fund
\$10,525
+0.11%

Gold
\$10,123
+0.32%

DRIVE/CGRAW HILL

Data on this page are as of market close Wednesday, Aug. 14, 1996, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of Aug. 13.

Mutual fund returns are as of Aug. 9. Relative portfolios are valued as of Aug. 13. A more detailed explanation of this page is available on request. r=revised

NEEDED: TOLL PLAZAS ON THE I-WAY

On Aug. 7, America Online Inc., the world's largest online service, went dark for 19 hours. The system crashed while AOL was upgrading its equipment to deal with the skyrocketing demand for Internet connections. Deprived of E-mail and connections to the World Wide Web, users complained bitterly, making the front pages across the country.

While it's unlikely this bug will be repeated, the AOL outage is a warning for the entire Internet. The demand for Internet-related services is soaring faster than anyone predicted just a couple of years ago. Every Internet company is being forced to add capacity to handle the mushrooming volume of E-mail messages, Web pages, and video.

But upgrading a complex network like the Internet is not as simple as buying a bigger refrigerator. It's like adding a room onto your house while you are living in it. The process is noisy, messy, and disruptive. Moreover, building more capacity won't solve the Internet's congestion problem. Adding bandwidth will only encourage more people to get online. Net engineers are finding out what transportation planners have known for years: Building a new road to alleviate traffic jams simply attracts more cars. So after the new road is finished, traffic remains just as sluggish.

In the case of highways, the best solution for congestion is to build more roads—while charging cars and trucks for usage. This is done both directly, by levying tolls, and indirectly, by taxing gasoline and diesel fuel. Such usage fees keep the congestion under control by providing an incentive to drive less, and they generate funds to build and maintain roads.

It's time for Internet users to start paying for usage. Right now, most subscribers pay a set charge for a connection, not according to the amount of data they send—but that's changing. Already, the largest Internet providers are beginning to bill smaller providers for handling their data. Soon, these fees will trickle down to individuals. Forcing Net advertisers to pay for huge broadcasts of messages will cut down on junk E-mail. And just as trucks pay more in tolls, heavy consumers of bandwidth such as videos and phone calls should pay more. That will discourage extravagances like broadcasting rock concerts over the Internet.

The shift won't be easy. Nobody likes tollbooths or gas taxes. But if the Internet is to thrive, that's what is needed.

THE NEW FACE OF STRATEGIC PLANNING

So far, the 1990s have been the decade of downsizing. But the era of the chainsaw may be nearing its end. At companies such as Procter & Gamble, Sears Roebuck, and Hewlett-Packard, the new emphasis is on strategic planning:

that is, identifying and shaping new markets. More managers are turning into architects and carpenters, visualizing and building rather than cutting. And there is a whole new school of management gurus who exhort companies to focus on where they are going, rather than where they are today.

The biggest benefit of strategic planning is its stress on growth. Many companies are nearing the limits in their current markets. Strategic planning creates an atmosphere that encourages managers to look for new opportunities, rather than simply cutting a few more workers.

But the danger of strategic planning is that it can lock companies into a particular vision of the future—one that may not come to pass. Once-attractive markets may not fulfill their promise, while new industries can arise suddenly. Today's strategic plan may be tomorrow's garbage.

That poses a quandary for corporate executives: How to plan for the future when the future changes so quickly. The answer is to make the planning process more democratic. Instead of relegating strategic planning to a separate staff, as in the past, it needs to include a wide range of people, from line managers to customers to suppliers. Top managers must listen and be prepared to shift plans in midstream, if conditions demand it. Achieving a balance between flexibility and planning is the best way for both Corporate America and the economy.

SHINE THE LIGHT ON MUNI DEALS

The Justice Dept. won a criminal verdict on Aug. 9 in a case that has rocked the municipal-bond industry. A jury in Boston found former Lazard Frères & Co. partner Mark S. Ferber guilty of fraud. Ferber, a Democratic political aide turned investment banker, failed to tell state officials that he and Lazard were receiving millions of dollars under a table from Merrill Lynch & Co. to help Merrill secure business. Ferber faces five years in jail for each of the 58 counts on which he was convicted.

The Ferber verdict may deter other would-be Wall Street crooks, but it will not remedy the continuing lack of disclosure in the \$1.3 billion muni-bond business. A 1994 rule limits—but does not eliminate—campaign contributions by municipal bond underwriters. Muni-bond executives still find ways to funnel campaign contributions to government clients. Late last year, the SEC took a giant step forward by implementing rules requiring issuers to disclose new information about their ability to repay. But municipalities and underwriters can still hire politically connected consultants without disclosing their financial interests.

Regulators should not stop now. Stronger disclosure of political activities by underwriters and their consultants is still needed. And more detailed information about the risks of muni bonds should become standard, as it is for corporations. These steps could bring the muni-bond business close to what it ought to be: an open, competitive market.

